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# ROYAL COMMISSION

ON

# TAXATION

## HEARINGS

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# THE ROYAL COMMISSION ON TAXATION

Hearing held in the Centre Court Room, Exchequer Court of Canada, Supreme Court Building, Wellington Street, Ottawa, on Monday the 2nd day of December, 1963.

## COMMISSION

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## RESEARCH DIRECTOR:

PROF. D. G. HARTLE

## SECRETARY

MR. G. L. BENNETT

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## INDEX TO EXHIBITS



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Ottawa, Ontario,
Monday,
December 2, 1963.

---On commencing at 9:30 o'clock a.m.

THE CHAIRMAN: We will now proceed.

THE SECRETARY: Mr. Chairman and Commissioners, the brief being presented this morning is from the Canadian Metal Mining Association, together with a supplementary brief from the Mining Association of British Columbia. Mr. V.C. Wansbrough, Vice-President and Managing Director, Canadian Metal Mining Association, will give a few opening remarks and will introduce his colleagues who are here before you.

I should like to enter this brief into the record as Exhibit No. 273, with the supplementary brief as Exhibit No. 274.

---EXHIBIT NO. 273: Brief of the Canadian Metal Mining Association

---EXHIBIT NO. 274: Supplementary brief by Mining Association of British Columbia.

THE CHAIRMAN: Good morning, Mr. Wansbrough and gentlemen. Before we start on this submission, I would like to introduce to you the Commission, whose names are all indicated. Then you will introduce yourself to us.

This morning I have requested Mr. Stewart, our legal advisor and counsel, to lead us into the questioning. We will probably have a few questions ourselves, but the quality of your submission and the technical aspects of taxation of your industry are such that we thought we would do better to leave it to Mr.

Stewart than just proceed ourselves.

We have all read the submissions with a great deal of interest.

Perhaps you would care to speak, Mr. Wansbrough.

MR. V.C. WANSBROUGH (Vice-President and Managing Director, Canadian Metal Mining Association): Mr. Chairman and Commissioners: My remarks are only to say thank you, and to identify the gentlemen who compose our delegation, whose names you have before you on the list, with the exclusion of two whose names have to be added.

I should like to introduce Mr. W.B. Dix, Vice-President and Treasurer, McIntyre Porcupine Mines, Limited, and Chairman of the Tax Committee of the Canadian Metal Mining Association. Next to him sits Mr. J.P. Coristine, of the Tax Department, Iron Ore Company of Canada. Then there is Mr. C.R. Elliott, Secretary-Treasurer, Cassiar Asbestos Corporation Limited and Mr. D.A. Foster, Treasurer, Quemont Minining Corporation Limited and Geco Mines Limited. Then there is Mr. C.H. Mitchell, who is submitting a supplementary brief.

In the second row, there is Mr. J.D. Taylor, Assistant to the Comptroller, the International Nickel Company of Canada, Limited, then Mr. J.C. Parlee, Vice-President, The International Nickel Company of Canada, Limited; then Mr. J.R. Bradfield, President, Noranda Mines Limited. Then Mr. R. Campbell, Vice-President Falconbridge Nickel Mines Limited; and next there is Mr. J.S. Row, President, Kerr-Addison Gold Mines Limited

and President, Canadian Metal Mining Association.

Next to him there is Mr. Ian C. Campbell, Secretary-Treasurer, Asbestos Corporation Limited, and here representing the Quebec Asbestos Mining Association. At the end of the second row there is Mr. W.J. Bennett, Vice-President, Iron Ore Company of Canada. In the extreme corner of the room there is Mr. N.Edmonstone, Vice-President and Secretary-Treasurer Steep Rock Iron Mines Limited, who is accompanied also by Mr. J.R. Tolmie.

In view of the remarks you made concerning the way in which the questioning will be handled, might I suggest that the questions might be generally sent in my direction and I will attempt to field them and distribute them. Will that be satisfactory?

THE CHAIRMAN: That will be perfectly satisfactory. Mr. Stewart, I think we might proceed.

MR. J.L. STEWART, Counsel to the Commission: Gentlemen, I would like to get right into a discussion of some of the features of Canadian taxation of your industry.

I would like to deal with a number of points I have in mind, in particular, the three-year exemption, the question of pre-production expense, the question of capital cost allowances, the question of depletion, including shareholders depletion and the question of the exemption to prospectors.

I would like to take these one by one and to start with the question of the three-year exemption.

THE CHAIRMAN: Before you do, would it be

helpful and expedite our hearing if, at such time as you finish each of those headings, you pause and allow for it to be completed before going on to the next one?

MR. STEWART: Mr. Chairman, I think that would be very appropriate. I shall start with the three-year exemption. This is a feature of the taxation of your industry which, as I understand it, is provided for by sub-sections (5) and (6) of Section 83 of the Income Tax Act, and Section 1900 of the Income Tax Regulations. Are these the appropriate and relevant provisions?

MR. DIX: Yes.

THE CHAIRMAN: What section of the Income Tax Act?

MR. STEWART: Section 83, sub-sections (5) and (6), sub-section (6) being simply the definition section, in which the word "mine" is included and is defined. It is also indicated that "production" means production in reasonable commercial quantities.

On page 14 of your brief, that is, the brief of the Canadian Metal Mining Association, you suggest that this tax exempt period does not begin until I think a mine has reached 60 or 65 per cent of its rated capacity. I take it that statement is based on the current assessing practice of the Department.

MR. WANSBROUGH: I think we might ask the Chairman of our Tax Committee to speak first to these questions. They are questions which many others may like to speak to also.

MR. DIX: The three-year exempt period in mind of course must have a length of time during which

its production is rated, very often one that does have what we call a mill run. The administration used to consider six months from the start of milling as a reasonable period for breaking in production. However, I understand that in recent years the period during which a mine might be in commercial production but not be in commercial production in accordance with the provisions of the Act, has been a varied one and usually they consider that when a mine, if it is, say, a 1,000 ton mill, when it reaches a normal production of 65 per cent of that amount, it is deemed to have then reached commercial, or, should we say, economic production.

MR. STEWART: So that the time when the three year period starts may in fact be more or less than six months after production actually begins?

MR. DIX: Yes, I think that is correct, counsel. Some of our delegation here may have had their feet a little closer to that particular job and I am sure they may be glad to say something on that subject, from that point. I think Mr. Campbell might do so.

MR. R. CAMPBELL: I think that is correct. It is the production level, rather than the time, that is the factor.

MR. STEWART: Thank you very much. Now, suppose we have a particular property which contains two or more ore bodies and on that particular property one of the ore bodies is developed first and comes into production first; and then at some subsequent stage work begins on production from the second ore body, is it the practice to treat that second ore body as a new mine

for the purposes of these provisions?

MR. DIX: Your remark would suggest that we might have the most ideal situation, in which an ore mine might have two ore bodies discovered and ready for exploration and development almost immediately. That certainly would be a delightful condition. But, basically, in mining one develops the first discovery first. It could be that after you get your shaft down and have a look and test of the ore body underground, your subsequent surveys and drilling or your surface geophysical exploration may have discovered another ore body in the same area. That exploration and development of the second ore body, and as it turns out, as I understand your question, the possibility is that that second ore body may be the richer in grade or perhaps greater in tonnage than this ore body which has been explored and developed; and the question is now: "Which do you develop first". Is that the type of reasoning I see in your question?

MR. STEWART: No, I do not think I was taking into account which was the richer or likely to be the more productive of the two. You will find, Mr. Dix, that many of these questions of mine indicate a remarkable lack of knowledge of how your industry operates. However, what I was getting at is this. Let us suppose that in one way or another you have determined to bring one ore body on a particular property into production; and you therefore become entitled to the benefit of this three-year exemption in respect of that ore body. Then, at a later stage, for one reason or

another you proceed with the development of the production from another ore body on that property. Now, does the department in fact treat that second ore body as another new mine and give you the benefit of another three year exemption in respect of it?

MR. DIX: Yes, I can see now the difference between your question and what we were talking about before. Here is a case as to whether the second ore body you speak of happens to be the second mine or the first mine. This is not quite what happens to be determined by the Department. There has been many problems involved in ascertaining whether a particular ore body in a particular mining area is in fact a new mine.

I do not think there is any great problem in whether in fact you do have a new mine. The facts that the Department used are related to shaft openings and whether you have a separate unit. These are questions of fact, which very often we have difficulty in trying to assess. But they are certainly not problems which are unsurmountable.

MR. STEWART: Then I take it that somewhat similar considerations would apply if, after opening up and obtaining production from one particular mine, the company acquires an adjacent property which is found to contain another ore body, which is then developed and brought into production. I suppose in that case the problem might be less difficult, because that ore body is on property which was not owned or did not belong to the producer at the time the first one came into

production?

MR. DIX: That is right. Might I perhaps give you a very good example of the question that you proposed there, Mr. Stewart?

MR. STEWART: Yes?

MR. DIX: Our own mine, which is a gold mine, McIntyre in Timmins, has been in operation since 1911. After 50 years, during which time mining has followed reasonably narrow veins down to 8,000 feet in depth, which is a long way underground -- after 50 years, with an exploration program into the area of the property, which was not conducive to finding gold bearing veins in the past, but where some very old drill holes did have traces of copper, when this exploration program was underway a new ore body was discovered, which is a fairly large low grain copper ore body. Here in part of the Porcupine Gold cap, right between the veins of the Hollinger and McIntyre, was discovered the copper ore body. That is after 50 years of operation. One could hardly say "Here is a new mine". Afterall, the mine has been there for 50 years but where the mine is a new one is of course a question of fact. We did not consider it a new mine, we did not apply for exemption as a new mine. The only distinguishing characteristics it had were sufficient to warrant its consideration as a separate unit for the purposes of E.G.M.A., if the costs of the copper mine or copper area were reflected in the production of costs for gold, for the purposes of the Emergency Gold Mine Assistance, as calculated.

MR. STEWART: Thank you very much for that

useful explanation. Suppose we had a different type of situation where a particular ore body had been developed on the open bed system and it was then concluded that underground mining should commence. Would it be arguable that in those circumstances the underground operation constituted a new mine.

MR. DIX: No, no. Perhaps Mr. Campbell would deal with that.

MR. I.C. CAMPBELL: This is common in the case of asbestos mining, in particular, in cast or quarrying metal, but as the ore goes down in depth it becomes uneconomical and has to be tackled by another method. In no case has it ever been considered as a new mine, although the mode of operation has changed.

MR. STEWART: I have before me a book, with which I am sure you are all familiar. It is entitled "Mining and Mineral Processing in Canada". This was one of the studies which was prepared for the Royal Commission on Canada's Economic Prospects, in 1957. It was prepared by Mr. John Davies and others. At page 361 of that book -- I am reading now from Appendix C, which is entitled "Federal Taxation on the Canadian Mining Industry" he is dealing there with the type of situation I have just been asking you to comment on, that is, how the three-year exemption has been administered, when particular situations of the sort I have described have developed. He says this:

"These problems, however, have been eased by a policy of giving the exemption an exceedingly

liberal interpretation, so as to minimize its incentive effect, a policy which has been greatly facilitated by the general flexibility of the Canadian tax administration."

Would you have any comment on that, or would you agree with that or tell us what you think about it?

MR. DIX: I would say generally that that is incorrect as to the conditions that exist today. The Department are following a very close line of definition of new mines. That may be because of two conditions. In the first instance, there is the period during which a new mine could come into existince for the purpose of exemption from tax, and this was limited to a period. Therefore, if you did not rush in and get your mine into production within the specific period then of course you could not qualify. There then was an end result. That may have had some effect, but I think that basically the Department is following a very strict rule now with regard to classifying an operation as a new mine for the purpose of Section 83(5) of the Act. I think most of us would agree with that.

THE CHAIRMAN: Perhaps, Mr. Stewart, the author has no regard to the non-deduction of development expenses and depreciation during the three-year period. Would that be the case?

MR. STEWART: No, Mr. Chairman not in this particular section.

THE CHAIRMAN: It is just the date of

commencement?

MR. STEWART: Yes, if that has been a new mine, and if that has been the action of the Department.

I would like to switch over to the view of the court and ask you if you have comments on some recent decisions which seem to have had a liberalizing effect. The first one was the North Bay Mica case, which was decided by the Supreme Court of Canada in 1958. As I understand it, the effect of that decision is that a mine may be abandoned, but that, if it is then reopened it may qualify as a new mine for the purposes of this exemption. Would you agree with that analysis?

MR. DIX: I am not too familiar with the North Bay case. There may be others on our panel who are familiar with it. If a mine ceases to become a mine, it must have been uneconomic, it must have been shut down for reasons best known at the time. If by chance another ore body is found at a later date, I presume then some other interest must have come into the picture and developed it.

In that case, I think there would be very good reasons for considering "Here is a new mine coming into production." This is good for the country, it is producing new wealth. I can quite see where there would be some liberal attitude with regard to whether a new mine had been found.

MR. WANSBROUGH: I should like to add one word there. I think it is a rather extraordinary and rare instance that you have picked on, and that Mr. Tolmie might be permitted to say a few words about it,

and dealing with what happened there and the reasons for it.

MR. J.R. TOLMIE: I am not familiar with the length of time during which it was closed. It was closed for a considerable period and considered abandoned and the economics of the place and the geology warranted a fresh exemption of this interest. This has been true of one or two other cases that have been accepted by the Department, administratively as new mines. There is one copper mine in the centre of British Columbia, which Mr. Mitchell would know about, which has been closed for twenty odd years, and the workings were filled with ice, but it was chipped out and re-examined. Due to more modern approaches to mining and the revaluation of copper, this became a feasible new product and was accepted as such under the new mine tariff.

MR. CORISTINE: I think the Department takes the position that underneath the mine is an ore body but also there are the facilities required to work it. So, even if you have an existing mine that may have been abandoned, if a new company comes in to develop it and spends a considerable amount of capital on developing it, it becomes in fact a new mine.

MR. BRADFIELD: In this case, if I recall correctly, they did not get the three-year exemption originally.

MR. STEWART: I think that is probably so.

THE CHAIRMAN: Mr. Stewart, when these gentlemen refer to the "Department" are they referring to the Department of National Revenue or the Department

of Mines, or both?

MR. WANSBROUGH: I was really actually referring to the Interdepartmental Committee on Mines and Metals of the Department of Finance.

MR. STEWART: The second decision I should like to mention is a decision of the Supreme Court of Canada in the earlier part of this year, in the Hollinger North Shore case, the effect of which, as I understand it, was that royalties which are received during the three year period, at any rate in the type of case that the court was there concerned with, are income derived from the operation of a mine and therefore entitled to the benefit of the exemption. Is that the effect of the decision?

MR. BENNETT: That is the effect of the decision, yes.

MR. STEWART: Was that regarded by the industry as a material extension for the benefit of sub-section (5)?

MR. BENNETT: Certainly, it would be regarded as such by any one in North Shore.

MR. STEWART: Now, gentlemen, you suggest in your brief -- and you document this in Appendix 2 to the brief -- that the three-year period should be increased, that is, where mines are brought into operation and in remote areas of Canada. It is Appendix 2 to the Canadian Metal Mining Association brief, which refers in particular I think to the area north of 57 degrees. I think that in the Mining Association of British Columbia brief they put it rather differently. They suggest that the facts of the particular case should

be looked at and the exemption period modified or governed accordingly. Would it be a fair summary of your views on this regard to say that you think this should be done because of the higher costs of finding, developing and operating mines in the type of conditions you are dealing with?

MR. WANSBROUGH: Might I make a comment there, Mr. Stewart. The original thesis which was raised before the Royal Commission on Canada's Economic Prospects was thinking in terms of using latitude to determine the degree of remoteness. However, Mr. Mitchell has pointed out in his brief on behalf of the Mining Association of British Columbia that he is dealing with the question of remoteness not only in the question of terms of geographical distance but in terms of accessibility. We have one person here who is extremely familiar with this matter, in the person of Mr. Elliott.

MR. ELLIOTT: I might say that Mr. Connell, in submitting that brief, had two things in mind in fixing 57 as the latitude -- or perhaps three things.

First, there would have to be some starting point. The latitude 57 was a fairly arbitrary figure, north of most of the operating mines, and north of that line very little industry possibilities offered, other than the mineral industry.

I agree entirely with what has been said by the British Columbia brief, in that remoteness is the final analysis, the key thing here.

The other thing Mr. Connell had in mind was that the question of development of these northern areas,

as I have said, is dependent upon the mineral industry. That was his main theme. He has been a pioneer for many years in exploring remote areas. It must be understood that every mining company is primarily an exploration company. You will find that anywhere in Canada that offers any possibility of minerl discovery, but to warrant that there must be some justification of spending money that is necessary to bring these mines, if are found, into production.

At Yellowknife you have two gold mines, actually there are three or four. The main one is the Giant. They were brought into being largely because they were in some degree accessible. If you depart from that very far, you are out in the wilderness again.

Lots of exploration has taken place but no one has seen fit to do very much about it, beyond the individual prospector who is looking for a plum.

In the Yukon, to give this specific example, we have developed there -- or at least we have discovered there a deposit of considerable size. But that mine will not be brought into production in the foreseeable future with the present exemption, simply because of the cost in getting that production to a point where it is competitive in the market. In this particular case, it means Vancouver. You have to take $50.00 right off the price of your product to get it down to the point where you can sell it.

That means in this case your mine has to be at least 50 per cent better than any other mine in the company.

If that particular deposit I speak of were in Quebec or in the eastern provinces where most of the asbestos mines are, or down in southern Vancouver close to the seaboard, there is no question it would have been in production long ago.

To open up, to encourage development, of deposits in these remote areas, you have to give the fellow who is going to do it an opportunity. Mining generally is a risky business. Whoever goes up there to open up the deposit, even if it is pretty good, has to be willing to take risks many times greater than the normal risk in mining and developing in the more accessible parts of the country where rail or water transportation is within a reasonable distance of the finding of the mine. In that case it is not a great problem to develop roads or railways, or what have you, to make that an economic proposition.

MR. STEWART: I would like to be sure that I understand this. I think I do. We are talking now about this present three-year exemption, not of course of the period beginning with the discovery of the product. We are talking about the period commencing with the bringing of the mine into production in reasonably commercial quantities, so that theoretically we could discover something pretty attractive or in a remote area and it may not come into production, I can understand that, for ten years, until the means of getting the product out had been developed. But it is not until this has all happened and until your mine has been developed and come into production, that the

exemption period begins. Now, why, in the circumstances, do you need a longer period there than is presently provided?

MR. ELLIOTT: To start with, relatively, it is going to take longer to get back some of your money. If you have not got some prospect of getting back some of this risk money that you have laid out, necessarily you will have laid out a considerable sum before you can begin to get transportation, and in that risk it may go with the wind and very often does, as I know very well. But the prospect of a successful operation is developed and being brought into production, has a better chance of being financed if the people putting up that money have a reasonable expectation that the first floor or the mine will all be available for the ultimate development of the mine -- to develop a mine you must in a remote area not only have transportation but everything from churches and schools to hospitals, to say nothing of the mining plant and the treatment plant. There has to be housing and all this has to be borne, and at the early stages before you have got a dollar out of it, you are faced with a large amount of expenditure of that nature, just to house your people. You cannot mine without that.

MR. STEWART: Therefore,does it come down to this type of consideration, that you have the increasing investment for a considerable period before you can get started on production,and that once you have got into production, because of inaccessibility or production costs going up higher and general expenses going up

higher, in the more remote property.

MR. ELLIOTT: That is correct, and after the mine is in production you have still a considerable capital expenditure going on. You start off with a minimum and after that you have still considerable capital provision to deal with, to provide the amenities of life for the people there, which they will demand if they are going to stay there.

MR. STEWART: During the course of our discussion I am going to ask for information about the situation in the United States in particular, and possibly in other countries. As far as I know, there is nothing in the United States which corresponds to this three-year exemption which we have in Canada. Is that the situation?

MR. CORISTINE: That is right. There is no three-year exemption in the United States.

MR. STEWART: You mention in your submission, in the current bill that there is provision for a three-year exemption in a limited field in Canada. My recollection is that in the field of the cooperatives there is also a three-year exemption. But this exemption for the mining industry is one, I take it, of great importance. It does not apply to the other extractive industries in Canada or to other industries in Canada at all, with these two relatively minor exceptions. Is that the fact?

MR. ELLIOTT: That is correct.

MR. STEWART: And you obviously regard this exemption as a great stimulus to the exploration and the

development of new mines in Canada?

MR. ELLIOTT: I would like to say that the development of the mining industry is dependent on the discovery of new ore bodies, which are not easy to find and which need a good deal of searching. In the first place, the discoverer has to be assured that when he finds a plum he is going to get it and a three-year exemption puts some dressing on it and makes the plum look more attractive.

MR. STEWART: Then I take it that during this three-year period it may be possible at any rate to recover on a tax exempt basis a very substantial portion of the investment which has been made in the mine?

MR. DIX: Yes, I think that is generally true. I think that is one of the intentions of the exempt period. The basic stimuli that the three-year period provides to the industry is one which is common, not as a matter of economics but as a matter of encouragement, for the mining industry. I think you have to know what mining is, what the difficulties and risks are. Sometimes, as I said last night, I wonder why we ever got into it at all. However, there is always a group of hardy people who are willing to explore and to take risks and this is something which is of course particularly of concern to Canada because of its vastness. This is basically one of the major incentives to the mining industry, that I think we will always have people who are willing to explore and risk money and get into the bush and look for new mines -- provided that when the pot of gold at the end of the rainbow, to use a simile,

is not eroded away by very onerous taxation principles. The impetus which we have had in the past 50 or 60 years for mining in Canada has been based on a tax program which has definitely worked. I do not think there is any question about that. The stimuli with the three-year exemption has been certainly of great value to the industry and I certainly hope that it will be something that will not be fiddled with in such a way as to make it less attractive to the mining industry generally. Because when we are planning our exploration program, it is very nice to know that if we find one, that the income for the first three years is not going to be taxed. That gives us a chance to get a new mine on its feet. It helps it to grow more quickly. If there is a stable mining operation there, it certainly gives it the stimuli to get it into that position. Basically that is what it does to the minining industry. It is a most important incentive to us.

MR. BRADFIELD: You have been talking about the position of mining in the United States. I feel we have much more activity in Canada than there is in the United States in finding new mines. All the American companies that I know have exploration departments which are very active in this country and particularly in provinces where there is still some incentive, that is, more incentive than in other provinces -- whereas there are very few Canadian companies doing exploration work in the United States.

MR. STEWART: Thank you very much.

MR. WANSBROUGH: May I have one word, before

we go on, Mr. Stewart. If you are speaking in particular of the beneficial and stimulating effect of the three-year tax exemption period, there is a general line of argument which will apply to every form of incentive, as the others which you mentioned earlier. We have the statement here by a senior official of the Canadian government, which expresses the view very well. If you have no objection, because this expresses the view so well, I should like to read it, for the purposes of having it put on the record.

MR. STEWART: If it is lengthy, we might accomplish the same result by filing it as an exhibit.

MR. I.C. CAMPBELL: I have it, but I am afraid to submit an exhibit, because it is part of a brief to another Royal Commission.

MR. STEWART: How long is it?

MR. CAMPBELL: It is only a couple of pages. With your permission, I will read it. It is as follows:

"These policies have been summarized by Mr. Keith Buck, Chief of the Mineral Resources Division, Department of Mines and Technical Surveys, in an address before the United Nations Conference on the application of science and technology for the benefit of less developed areas, held in the spring of 1963, in Geneva. We quote the following:

'I have attempted to describe

the formula which has resulted in Canada becoming one of the world's largest producers of mineral wealth, close to $3 billion in 1962.

'1. Security of land tenure. At each state of exploration, development and production, the rules of the game must be clearly defined and constantly and impartially implemented.

'2. Generous disposition of mineral rights. Mineral exploration has a high element of risk. The taking of this risk should be made as attractive as possible. The economic return to the nation can be obtained at a later stage.

'3. The granting of tax incentives. In Canadian experience, this is the main ingredient. It can take many forms. In Canada, it consists of:

(a) a three-year tax-exempt period for new mines;

(b) a 33-1/3% depletion allowance, in perpetuity;

(c) a provision permitting recovery of exploration and preproduction expenses;

(d) freedom from capital gains tax;

(e) special excise tax and customs tariff provision for mining equipment;

(f) incentives for further processing;

(g) other special tax inducements as circumstances might warrant from time to time.

All these provide permissive recovery of capital investment, giving recognition to the intrinsic risks of mineral development. In principle, also they could provide insurance against the changing attitudes of changing governments.

'4. Government services. The more important of these services are:

(a) Basic geodetic, topographic, hydrographic, and aerial photographic maps;

(b) The geological and aerogeophysical maps so essential to intelligent private exploration;

(c) Ore Dressing Research for mineral discoveries;

(d) Resource - economics surveys and studies;

(e) Mining access roads, railroads, airstrips, docks, harbours, housing, telecommunications -- all under certain circumstances.

'5. Bounties to assist in the early stages of development of primary industry.

'6. Subsidies. Our experience with subsidies, like that of many other countries, has not been a happy one.

'7. Government financial participation has been, but only rarely, employed in Canada, mainly in times of strategic necessity.

'8. Commission of Enquiry into matters of broad regional or national concern have occasionally led to the development of specific mineral policies.

'9. Provision of university-trained people in the mineral profession and of mineral technicians at the next lower level.

In summary, Canadian experience indicates that enlightened, consistent government policy is needed to encourage mineral exploration, development and exploitation, that the special needs of the mineral industry are best met by incentive-creating legislation; that corporation affiliations may be most useful in both the provision of capital for mine finance and the provision of assured

market for primary mineral output;
and that a supply of trained engineers,
scientists and technicians is essential
to a sound and lasting mineral
development program.

The development of a nation's resources for internal use and for export is a basic means of providing new wealth. In the case of less-developed countries, mineral development is a logical first step toward mineral self-sufficiency; it permits the acquisition of foreign exchange; it enables the development of technical 'know-how'; and it promotes the development of related resource-based secondary industry.'"

THE CHAIRMAN: Thank you very much.

MR. STEWART: Thank you Mr. Campbell. During this three-year period we are talking about it is not necessary for the company concerned to take any of its pre-production expense under Section 83a of the Act in capital cost allowances. Is that the situation?

MR. WANSBROUGH: That is correct.

MR. STEWART: I should like to ask this. From the point view of the proper and best mining practice, you will know much better than I ever will what is involved in the expression. Has this exempt period any adverse effects? As a layman, thinking about it, I cannot help wondering whether it may have

the effect of delaying production in a particular situation. I cannot help wondering whether, in the course of the three years steps may be taken to maximize output which could not be in the best interests of the operation from the long term point of view. In other words, that production procedures might be affected. Now, would you comment on this and tell the Commission whether there is anything in considerations of that sort?

MR. DIX: Mr. Stewart, this is a question which I might deal with in several parts. If we take this one relating to the maximizing of profits over the exempt period, to the disadvantage of the economy or the operation of the mine as a whole, I think I can quite safely say that the basic economics of an operation are going to determine what is the maximum amount of production that will come from any particular new mine. Since you mention it, I am just assuming you are referring to the exempt period which deals with new mines. Reading in exploration and prospecting into the same question, I think separates it widely, because a new mine is so busy getting itself into production, getting its own mine ready for commercial production, that it seldom if ever has any funds which it wants to spend during that period for exploration and prospecting and development of new mines, such as Section 83a contemplates.

There is quite a difference between pre-production and this prospecting and development exploration allowance, which is primarily for mines that

are in production and are in exploration.

Now, a mine comes into production on basic factors, which are mine factors -- that is, the size of the ore body, its grade, its nature, its location -- and by location I mean its location in the ground. These are all factors which will determine a number of things -- the tonnage rate at which it should be brought into production and also the type of operation, the type of mining.

These are mining economics. Basically, sound engineering practices will determine how much and how soon a mining operation should be brought into production.

I think there is one golden rule in mining, which is that you should get the mineral out of the rock as quickly as possible. The sooner you can get it and the less you have to do with it, maximizes the profit on that particular mineral. I think that is basic and sound in all mining.

The relation of timing, because of the exempt period, is something which I think is natural. By that I mean that since you have a three-year exemption period I do not think there is any question but that any sound mining program will maximize its taxable income during that three-year exemption period, but no sound mining engineer is going to maximize that production at the economic expense of its mining operation. For example, if new ore bodies warrant a 1,000 ton operation, no mining engineer in his right mind is going to bring that in by a 3,000 ton operation,

just to get in all he can in the exempt period.

MR. STEWART: If he knows or suspects the ore varies in grade, would there not be a human tendency to try to get the high grade ore out.

MR. DIX: No, it is not possible. It is the absolute opposite.

MR. STEWART: Why is that?

MR. DIX: Because the economics of your operation are such. There is the fact that you have a high grade ore, which means that you have many more tons of sub ore which can be profitable only because you have the high grade. That means that you have the product mixed. That is, assuming that the practical aspects of taking out those grades of ore can be mixed. Very often it is impracticable. If you just take out the high grade, you will never take out the rest of the ore. You have lost it for good.

MR. CAMPBELL: It could be feasible that if you were to go as you suggest, you would have lost the economic working of that mine in the three years and you would have lost a lot of the profitable margin of ore which is underlying the ore you have taken out.

MR. STEWART: That is what was concerning me.

MR. CAMPBELL: You have to take the whole life of the mine, as it is, and not consider just the three year period.

MR. ELLIOTT: I think the history of new mines which have been successful, has been one of increasing output rather than a large output. Most of them start off fairly modestly, for the simple reason that they do

not know how much ore they have to work out. As they develop those first years, they find out what they have to move, and justify the increase in capital. There is one mine right now in the process of increasing its output, though it has been in the tax exempt period for some time.

MR. STEWART: Could you indicate, or is it known, to what extent explorations at the present time are being carried on by branches of American companies, as opposed to Canadian companies.

MR. DIX: By "extent" do you mean how much is being spent on it?

MR. STEWART: I suppose that would be a natural criterion.

MR. BRADFIELD: I doubt very much if any of us can answer that question. As was said a moment ago, very large amounts are being spent in Canada by American companies, and I think it is in the record.

MR. BENNETT: I do not think it would be useful. What is happening at the present time, certainly in the case of my own industry, the iron ore industry, the capital is predominantly United States capital. This is an historical fact.

MR. STEWART: Historically, has this been done through branch operations or through subsidiary operations in Canada.

MR. BENNETT: You have a mixture there. For example, you have the iron ore company, where you have a new corporation with corporate shareholders, companies, steel companies, the Canadian Hollinger group and United

States steel companies. The latest one of course is Wabash, which is a joint venture of two Canadian steel companies and American steel companies. Here you have separate corporate identities in a joint venture. There are many varieties, depending on the circumstances, and there is any variety of corporate arrangements possible.

MR. BRADFIELD: As a matter of fact, they all set up Canadian subsidiaries, Canadian companies, to do the work.

MR. CAMPBELL: This is sometimes a requirement of provincial legislation, that mining companies operating within the province have to be incorporated within the province.

MR. STEWART: There is one aspect of this which seems to be important from the Canadian taxation point of view. If a United States company comes up here and carries on mining activity through a branch and gets a three-year exemption from Canadian tax, are we in effect not waiving Canadian tax on that income and permitting the American government to derive the tax?

MR. WANSBROUGH: I daresay there is something in our brief on this, and Mr. Coristine might like to deal with it.

MR. CORISTINE: I do not think that statement is correct, Mr. Stewart. It depends on the circumstances. Because of the greater depletion allowances in the United States and because of the rapid write-off allowed under the new guidelines in the United States, and because of the greater flexibility in determining tax income in the United States -- and I know what has

happened in the case of the Iron Ore Company, which has just such a company -- that the Canadian tax is governed. In other words, there is sufficient production. With the States there, there would be no tax paid in the States. There is very much more depletion allowance in the United States, because you can get it on individual properties, so that even in a year when the corporation might have a loss, it can still charge capital depletion on one of its properties.

MR. STEWART: I am interested in that statement and will come back to that later. There seems to be more than one school of thought on the relative liberalism of the American and Canadian depletion systems. I have read, and I will put it to you a little later, that the general effect of the two systems at the moment is about the same.

THE CHAIRMAN: This comes up on depletion rather than on the three-year exemption.

MR. DIX: Might I add one or two comments on your question with regard to the United States. I do not think we should allow our ideas with regard to some taxing benefits that the United States company might receive and operate in Canada, to cloud the benefits that particular operation has given for Canadians generally.

The fact that the funds have been spent in Canada and a new mining property has been developed, irrespective of the originality of the invested capital, then Canada is the gainer.

The new wealth which has been created, very

often 75 per cent of which creates new employment, new towns, new villages, new industries, all these things I think weigh heavily far on our credit side. I think that would minimize if per chance any foreign company has itself gained some tax benefit in its own country by reason of its operations here. I do not think that should be of any great concern to Canadians who have received the full benefit here.

MR. STEWART: Mr. Dix, I think that is logical, up to a point; but our general principle in Canada is that we tax non-residents who carry on business here, on business derived from their Canadian operations. That general principle seems to be reasonably logical. Here we have a case where both residents and non-residents are not going to be taxed for a three year period. This exemption may have an overall justification from the Canadian point of view but so far as the non-residents are concerned it may mean that whatever income tax is imposed on the operation during the three-year period is going to be imposed by a foreign government. It may be -- I do not know -- it may be that to overcome this, if there is a problem to be overcome, the exemption could be extended simply to Canadian residents, so that the foreign company which wants to come here -- and from what Mr. Bradfield has said I gather that many of them, and perhaps most of them, act through the Canadian subsidiary rather than the branch operation.

MR. BRADFIELD: Might I say that a lot of the American companies successful in establishing operations in Canada do not do that through staking of

property. Many of them acquire properties through purchasing some Canadian company and subsidiary group.

MR. STEWART: Is this before or after the three-year period?

MR. BRADFIELD: Before it.

MR. CORISTINE: If something has not the effect that the three-year exemption is lost to the United States, because as I say there are many off-setting factors in the United States, where mining companies have advantages they do not have under Canadian law and certainly in the case of the Iron Ore Company, we have a specific example. We have not paid tax in the United States and it us unlikely that we will, though we have through our subsidiary paid substantial taxes in Canada. It might be, in some cases, it all depends on the arithmetic of the finances of the company.

MR. STEWART: I can quite imagine there may well be an American taxpayer who has multiple operations and who is receiving income from a Canadian branch during this three-year period, which may not be in an overall tax paying position in the United States. Are you putting it to me that in the normal case, if this is the sole operation of the American corporation which has a branch here, that, during that three-year period, its deductions of one kind or another are going to exempt it from the United States income tax?

MR. CAMPBELL: It does not pay dividends during that period.

MR. CORISTINE: That is right.

MR. STEWART: I find it difficult to try to

keep up with Canadian taxation, without dealing with United States taxation, and I do not want to challenge what you have said, but it seems extraordinary.

MR. CORISTINE: It is a fact that there has been rapid amortization in the United States and now there are new guide lines. I think you can make the general deduction that there are sufficient deductions now in the United States to keep American companies substantially out of tax. Again, it depends on the individual company and on the operation.

Generally speaking, the three-year exemption does not get exported in the case of a branch operation.

MR. STEWART: Mr. Chairman, that concludes my questioning on that first point.

THE CHAIRMAN: All right. I have two lines of questioning here and I would think that other Commissioners would have some questions also. There is one point I would like to explore.

First, what is in fact the period which is allegedly a three-year exemption period? I do not believe it is three years at all: I believe it is something more than three years.

Secondly, I would like to see what is achieved by virtue of the three-year exemption, if it is possible to find that out. In this, I am not challenging the desirability of incentives in any way at all, but I think we in this Commission must look first at all at what is income, because this is a tax on income, and over and above that, the extent to which it is desirable to provide incentives -- and the incentives are really

provided simply by moving the tax from one group of taxpayers to another group of taxpayers -- and of course there are very good reasons for that.

If we want to develop national resources in Canada, the only point is to how far we should think of taxes passing from one group to another group or subsidies in the national interest.

As to this three-year exemption, the accounting for this requires that certain expenses be deducted during the three years, and certainly that other expenses be not deducted during the three years. Those not deducted are development and of course depreciation.

I think all these gentlemen would agree with me that for their own accounting purposes depreciation would be deducted during the three-year period and probably there would be amortization on development, also. It might be that that amortization would in the accounting require certain right-offs of what is taken for tax purposes. If that is true, those charges which are deferred beyond the three years and which in accounting would normally come within the three year period, are in fact an extension of that exemption.

I do not know how long that extention is, but I suppose it varies with every enterprise.

I have heard it explained that the advantage of this three-year exemption is to encourage new capital in the mines, and it is a very good thing to be able to tell prospective shareholders that they will not be taxed for three years. However, I think it would be better to tell prospective shareholders they would not be

taxed for five or six years, or whatever the case may be. It seems to me to be very logical, and I would like to know what the comment on that would be. Instead of it being a three-year exemption based on what I think is very weak accounting -- it may be suitable from a tax point of view -- I do not know whether that is true or not -- if you are accounting, you do not charge off depreciation and if it should be a five year period or a longer period based on strict accounting, which anyone would be prepared to say is fair accounting. Would that not be more realistic and a better approach to this problem. It would seem to me that it would be a great deal more useful to your industry to carry out the purposes for which you say the exemption is provided.

MR. DIX: Mr. Chairman, I think that to follow the line of thought with regard to your question, one would have to know the individual particulars with regard to many of these mines that have applied for and obtained the three-year exemption period.

If many of these companies had been required to write normal depreciation and pre-production as I think a differential between pre-production and current development, which normally would be charged off anyway.

During the exempt period there would be little if any profit which would produce taxable income and therefore the exempt period would produce little or no benefit to them.

Primarily, that is one of the reasons why the Department changed its administration of the exempt period from its original concept, where depreciation

was required to be deducted during the exempt period. Now, it is also true that, dependent on the economics of any particular mine, it is quite possible that the build up of pre-production expenses and capital cost allowances, waiting the end of the thirty-six month tax holiday, the taxable income is correspondingly reduced for perhaps a very subsequent period.

This is true, but in effect we are only postponing the tax ability of that mine. From that point on, we are not getting any free taxable income. I think others will probably want to answer your question, but for many of these companies I am sure there would have been no benefits during the three-year period, if they have been required to write-off the pre-production and depreciation on normal accounting, during that period.

THE CHAIRMAN: During those first three years, those companies made no profits?

MR. DIX: That is right.

MR. STEWART: I do not think your first point has really been discussed. Is this a three-year period or a longer period?

THE CHAIRMAN: I think I made a flat statement. I do not think I asked a question. I think I said it was a longer period, and I think I am happy to leave it at that, unless anyone wants to challenge it.

MR. DIX: The exempt period is thirty-six months from the time it comes in commercial or economic production. That is a statement of fact, subject to that time, the question whether this exemption from tax

is somewhat different.

If we add the two of them together, it is quite possible that a particular mine which has enjoyed a three-year exempt period might in effect be free of income tax -- not tax free, but free of the liability for income tax -- for a period longer than three years. A lot of that depends on the economics of the particular operation. If it is a very lucrative one during the three-year period, it will get into the tax bracket very quickly. If it is a marginal operation, it might go for ten years before it has taxable income.

THE CHAIRMAN: I think the average is of five or six years, whatever the case may be. It seems to me that it might be desirable to call it that.

MR. DIX: If you do that, you have to take things into consideration. I do not know, but I think that roughly half of the companies that have claimed under this particular section never completed the three-year period. You have to look at the industry as a whole, in order to determine whether three years is too short or five years is too long.

THE CHAIRMAN: That is what I had in mind -- and at the same time, had regard to good accounting.

MR. ELLIOTT: I do not think I could let that flat statement pass, because as Mr. Dix has pointed out, after the three-year exemption from tax liability is exhausted, there is a further period during which no tax is paid and it has the result of using up deductions available to the company in the normal course of events. It is not an exemption and if the company is profitable

as such -- if it is -- many are not -- that can become taxable in the first taxable period following.

Others may go on for some time and pay tax and at the end of the rated time, they have no write-off.

THE CHAIRMAN: I think we are on all fours. I think there is no contradiction. I am saying that this permits the deferment of items which, under good accounting, are not deferable. That was my first question.

We would like to have some evidence on this. I doubt if it is possible, and I think all I can say is that it certainly improves the prospect of getting the finance by way of the exemption. It certainly costs the government money to permit the three-year exemption and one has to weigh the disadvantages against the cost. In seeking to find out about the advantages I think I would like to ask the question, whether anybody knows of an instance, or two instances or more, where mines have come into being and the deciding point, when they got down to weigh the pros and cons -- the final deciding point is that there is a three-year exemption.

Would anybody have ever seen an instance where, if there were not that exemption, the mine would not come into being; but because there is that exemption, it has come into being. Is there any mine of that kind?

MR. ROW: I can think of one example. There is one very recent operation, which probably would never have gone into production except for the three-year exemption. After you get the shaft down and do some

exploration work underground sometimes you find more ore -- which I hope will happen in this instance. I know we have another one, an ore company, on the west coast which certainly we could not have dealt with if this provision had not been made.

We have one in a new town which looks to me as if it is a case where, without the tax free period, we would not have economic production. As it is, I think it will.

MR. EDMONSTONE: We have a new mine coming into production, or which we hope will come into production, but will not go into production unless it gets exemption.

THE CHAIRMAN: You mean to say that your decision will be against it unless it gets exemption?

MR. EDMONSTONE: It will not be all decision, but it is a decision of the consumers.

THE CHAIRMAN: Your profits are adequate during that period to justify going into operation -- is that it?

MR. EDMONSTONE: Not during that three year period, but it means so much to consumers that they insist on this incentive.

MR. STEWART: Can I ask if these consumers are shareholders in your company or is this a matter of price?

MR. EDMONSTONE: It is a matter of putting up the money.

THE CHAIRMAN: These are your backers?

MR. EDMONSTONE: Yes.

THE CHAIRMAN: Then they are the shareholders of the company -- the consumers?

MR. EDMONSTONE: I mean the consuming interests.

THE CHAIRMAN: The purchasers of the products?

MR. EDMONSTONE: The purchasers of the products, yes.

THE CHAIRMAN: The purchaser of the product will get the product at the price -- which he would not get if there were not the three-year exemption; and your reduction in price makes this project feasible, is that right?

MR. EDMONSTONE: Yes.

THE CHAIRMAN: But this is a tax on profits. It is there irrespective of whether it is tax free or fully taxed, there would be a profit -- it is this degree of profit that makes all the difference?

MR. EDMONSTONE: It is the degree of profit and the recovery of capital that matters to these people.

THE CHAIRMAN: Thank you. I get the point -- that the profit without tax is sufficient to recover capital that much faster than it would be if taxed.

MR. EDMONSTONE: The consumers who put up the capital want to see the capital back as quickly as possible.

THE CHAIRMAN: Those are shareholders who put up the capital.

MR. CAMPBELL: The financing group.

THE CHAIRMAN: The financing group and the

customers are the same people, in this case?

MR. EDMONSTONE: Yes. This has to be a large scale basis.

THE CHAIRMAN: I understand. Thank you. Those are all the questions I have.

COMMISSIONER GRANT: I have been wondering whether a three-year exemption influences a company to get into profitable production faster, so as to benefit from the income that is derived from production within that three-year period.

MR. CAMPBELL: I think markets are a more important consideration.

COMMISSIONER GRANT: The point going through my mind is this. If a given ore body calls for the placing of a mill on that property of a certain tonnage -- let us take, for instance, as I am not familiar with mining, that it calls for a 1,200 ton a day production, might there be a tendency to get into production earlier and to benefit from the income which could be taken in the first three years, to help the mining venture, rather than to sink your shaft and develop your underground to the extent where you could take out in say the third year of operation enough to keep your mill in full production every day.

MR. DIX: Mr. Grant, I think your question can best be answered by pointing out the practical limitations of getting into profitable production as quickly as possible. Again I repeat that the basic thing in mining is that the sooner you get the mineral content out of the ore, the more profitable that

particular mineral is. The practical limitations of course are in the nature of the ore body, and the markets for the mineral.

If there are ready markets for the mineral, for the metals to be produced, and if the nature of the ore body is such that it is flexible in operation, then, having determined the economic limits of extraction for that particular ore body -- it might be 1,2000 tons a day, which is a specific rated capacity of a mill -- then I think your question means that companies certainly who would be well advised in trying to get into profitable production as quickly as possible.

All these other things have to fall into line. You have to sink your shaft first, your shaft has to be of a size and nature sufficient to warrant the production of 1,200 tons a day, and the ultimate production from that area must be worked out, usually before you sink your shaft. You cannot take 2,000 tons a day out of a 1200 ton a day shaft. These things must be worked in advance. That is why I say the economics usually determine the time and the rated capacity for a particular mine. The grade of the ore determines its economics basically.

COMMISSIONER GRANT: I am perfectly satisfied, as long as the answer is that the three-year period is not being exploited from the point of view of taking out income in that period as fast as it can be taken out.

MR. DIX: I do not think the three-year period has been exploited at all. We certainly will maximize

our operation within the practical limits of mine economics. These are the major economics.

COMMISSIONER WALLS: I should like to discuss your second recommendation, with respect to extending the exemption to mines operating in remote areas. I am not just clear how you could define a remote area. I know it was suggested, I believe in some previous brief, that it was based on a certain latitude and I presume that in the case of a mine like Pine Point, it would be eligible for an extended period. Here you have a mine with a railroad now leading up to it, so that it is no longer an isolated or remote region. If the area alone is defined as being above a certain latitude that is not going to create more equity within your own industry, it seems to me.

I also believe that when we were up in Yellowknife there were a number of high grade gold mines there which were quite profitable and which were shipping semi-refined ingots out by plane. Would you call that, then, an isolated area, that would warrant a period extended beyond three years?

MR. ELLIOTT: A gold mine is an exception, in so far as the transportation of the product is concerned, in that you get a very high value, $100,000.00 which you can carry under your arm, if you are strong enough; but if you take $100,000.00 of lead concentrate, or for that matter lead pigs, you need something more substantial.

COMMISSIONER WALLS: Therefore, you would exempt gold and silver from the recommendation for an extended period for remote regions?

MR. ELLIOTT: I do not think that follows necessarily because even in the case of the gold mines they have to take in their supplies and all the other things and the transportation of the product alone is not the whole problem. I merely point out that small high grade mines which you have in mind have been able to operate first because they are high grade and secondly because they have a product which can be flown.

COMMISSIONER WALLS: I think you will agree with me that some tighter definition is required before any definition like this could be granted.

MR. ELLIOTT: I agree with you that determination of what qualifies for a remote area may present some administrative difficulties. When Mr. Connell selected 1957 he had that in mind, there was in Pine Point no railroad then and it was considered doubtful whether there ever would be. It was a practical measure that would fit most people, but obviously would leave out some who, as Mr. Mitchell has pointed out in his brief, are equally remote, and are equally in more southerly latitudes.

MR. MITCHELL: As you know, you could have a very unsuccessful mine very close to the United States border, near the ranges in British Columbia. I am sure Commissioner Walls is familiar with such incidents.

COMMISSIONER WALLS: Yes, I am.

MR. MITCHELL: If you take a mine situation on the top of the glazier and it is inaccessible and it will require a considerable assistance. A major road would have to be built to the project and there will be the

construction of one town and the expansion of another one. Under those circumstances, I think the operation of that mine is going to be extraordinarily difficult. There will be a lot of supplements here, even in the operative period. It is a not a high grade copper operation, it is touch and go. We might even have cited it to Mr. Carter, although we cannot do that. We may have cited one where there is no three-year tax exemption, and for that matter, no preferential three-year tax exemption, and it might be doubtful if that property would be brought to production.

COMMISSIONER PERRY: I was interested in the emphasis you put on page 13 in regard to the element of mine financing. Would this be a common feature of all new mine financing, and, if so, what form does it take? In the fifth paragraph, you say:

> "A major practical interest of companies in the tax exempt period is the cash flow. Many new mines are forced to borrow money to get into production."

MR. STEWART: Might I ask a supplementary question, Mr. Chairman. Was it not the case that when the uranium mines were being brought into production comparatively recently, there was a great deal of bond or debenture financing.

THE CHAIRMAN: That is correct.

COMMISSIONER PERRY: I know about the uranium mines. What I was asking was whether this was the general practice in the mining industry, to finance the

initial development on borrowed money and if so where do you obtain borrowed money? What form does it take?

MR. CAMPBELL: There is no fixed rule, Mr. Perry. It depends upon the particular project. As regards the amount of the capital that you borrow, some of it will take the form of equity, some in the form of long term bonds, some of them may be on the basis of marketing arrangements, or guaranteed sales.

COMMISSIONER PERRY: Might some be corporate borrowing from a parent?

MR. R. CAMPBELL: By "initial capital" do you mean initial development of the ore or do you mean the whole capital?

COMMISSIONER PERRY: I am just asking what your brief means when it makes certain statements.

MR. R. CAMPBELL: I know of one particular development, that is the finding of the material by diamond drilling from the surface. That I believe is done through equity capital. But the senior financing, I believe is very commonly done through borrowing, very frequently the sale of some form of debentures or bonds, and bank loans, sometimes, having been guaranteed by corporations; but I do not think under all these conditions it would be possible to bring any major operations without that type of financing.

Our company has brought in some new mines by borrowing on new mortgages.

COMMISSIONER PERRY: My impression is that not much of this is market financing.

MR. R. CAMPBELL: Thereis reluctance to give

away equity, and if you can borrow, so much the better.

MR. EDMONSTONE: In regard to some of these new mines, this is not available from the public offer. It has to be institutional money and even the big companies who will come in and put money up under marketing arrangements will go to the institution for the money. These institutions want to see a substantial cash flow, particularly in the early years. However, if this cannot be shown, then, good-bye.

THE CHAIRMAN: Thank you very much. We shall stand over for ten minutes.

---A short recess.

THE CHAIRMAN: Mr. Stewart, let us proceed.

MR. STEWART: Thank you, Mr. Chairman. Gentlemen I would now like to come to section 83a, to what is called there the prospecting exploration and developing expense, and to which I think has been referred to this morning as the pre-production expense.

I would like to deal first of all with the classification of the taxpayer which includes corporations whose principal business is mining or exploring for minerals and processing mineral ores. In the application of Section 83a by the authorities, have you any major problems in connection with the definition of pre-production expense? That is, are there any problems as to what does and what does not come within that category?

MR. DIX: Mr. Stewart, you mention pre-production with regard to 83a. Now, 83a is primarily

prospecting exploration and development expense. Pre-production, as I think I mentioned earlier, really has only relation to a new mine. The significant effect of Section 83a is in relation to mining companies who are operating mines. We have no serious problem from the administration point of view, as to what is prospecting exploration and ore development.

There are problems, but I do not think there is anything we could say that, as an industry, it makes it difficult to determine what is prospecting exploration and development.

Certainly a company which is producing metals, none of its expenses on its own property for exploring prospecting or development are Section 83a expenses; they are current expenses. The section 83a expenses are considered to be expenditures on property outside of exploration. That is the common term for it.

THE CHAIRMAN: What did you say that term was?

MR. DIX: Outside exploration. Did I understand your question right, Mr. Stewart?

MR. STEWART: I am interested in this. As regards the point that you have made, I am not sure that it really was an answer to my question, but let us explore your point first. You say that Section 83a permits the recovery of off-property or outside exploration and development expense?

MR. DIX: That is correct.

MR. STEWART: Now, why do you say it does not apply to similar expenses on theparticular property?

MR. DIX: The administration of property so

rule.

MR. STEWART: Let us go a little further, as I wish to be sure that I follow you.

MR. DIX: We are a gold mine and spend $100,000.00 on diamond drillers, looking for a new supply. That is an exploration of that particular mine. We spend $100,000.00, exactly the same amount, let us say, in the Province of British Columbia, also looking for a gold face. That $100,000.00 spent in British Columbia is Section 83a. The $100,000.00 spent on McIntyre mine in Timmins area is current expenditure. There is no relation between the two.

MR. STEWART: Let us suppose that you establish a competely new property or acquire a completely new property. Then you proceed with the exploration and development on that property. This is a section 83a expense?

MR. DIX: That is correct.

MR. STEWART: It is only after you bring that particular property into production that any further exploration or development on that property is treated as current expenditure? Is that correct?

MR. DIX: That is correct.

MR. STEWART: I follow that. In any event, I think that perhaps my first question did not take your distinction into account. In any event, I gather from what you have already said that you have no real problems at the moment in agreeing with the Department as to what comes under the expression "prospecting exploration and development expenses"?

MR. DIX: I would say --, industry-wise, I do not think we have any major problem. I would not admit that there are no problems, because when you deal with a complex section like Section 83a, in which a company creates today certain prospecting exploration and development on another company's property, in exchange for shares or something of that kind, it is in effect assuming the privileges of claiming that exploration as it is under the Act itself, rather than let that acrue as pre-production expenses for that company.

Then there is the problem as to whether these are the prospecting exploring and development expenses of the company. When you are actually in operation, such as building a mill, I do not think we could say that the expenses related to research, if a mill could be considered to be prospecting exploring or development expense, in the case of a new mine under these circumstances.

There are those areas, but I think that industrywise we have no major problems. Perhaps if there are, some of these gentlemen here would be glad to let you know about any individual problems which they may have.

MR. STEWART: I really assume that if there were major problems they might have been reflected in your submission. Now, could you tell us what types of expenditures are incurred during the prospecting exploration and development stage of a particular property and which cannot be recovered under Section 83a?

MR. DIX: I think it is an all-encompassing section. I do not think there are any -- there may be some, but if there are they are not of major consequence.

MR. STEWART: How important in your industry in the normal case is land acquisition cost, the cost of acquiring whatever interest you do acquire in a particular property?

MR. DIX: I do not think that would be important in our industry, in relation to this particular industry. We probably differ from other industries in that respect.

MR. STEWART: During this particular stage, if you expend money on depreciable assets, I think you recover those costs to the operation of capital cost analysis and not under Section 83a?

MR. DIX: That is correct, yes.

MR. STEWART: Then, under sub-section 3b of this section, which I take it is the one which is now the basic subsection for the purposes of the type of company we are talking about now, that is the company whose principal business is mining or exploring for minerals -- you can recover not only your exploration expenses in searching for minerals, but any drilling and exploration expenses which you incur in searching for petroleum and natural gas.

MR. DIX: That is correct, Mr. Stewart. There is quite a similarity between the nature of exploration for oil and the exploration for minerals, because they both deal with the ground.

MR. STEWART: I would like to make sure we are

on common ground as regards the effect of this particular deduction. I would like to put three or four propositions to you and make sure that you are in accord with them.

First of all, once we get past the three-year period, this deduction must be taken in the computation of income, to the extent that there is available income.

MR. DIX: That is correct.

MR. STEWART: Secondly, the deduction can be taken from income from all sources. Is that correct?

MR. DIX: That is correct.

MR. STEWART: Thirdly, the deduction can be carried forward for an indefinite period.

MR. DIX: That is correct.

MR. STEWART: Fourthly, there is no tax on production income until this particular expense has been fully absorbed.

MR. DIX: That would be correct as long as you have off-setting charges. There would be no taxable income.

MR. STEWART: Now, this may follow from what has already been said, on a point which the Chairman raised earlier. What would your views be on this proposition, that these costs that we are dealing with under Section 83a would ordinarily be considered to be of a capital nature and would not be directly deductible in the computation of income if it were not for this particular provision?

MR. DIX: What type of costs are you referring to, that would be classified under section 83a which might

be deemed to be capital costs?

MR. STEWART: Let us take exploration.

MR. DIX: We would never consider exploration to be a capital cost.

THE CHAIRMAN: Just a minute, Mr. Stewart, I find that exploration is capitalized on the balance sheet quite frequently.

MR. DIX: As cost of mining?

THE CHAIRMAN: I think so.

MR. DIX: Basically, section 83, as has been point out, is used by companies whose principal business is mining. You must be in the mining business in order to claim these operating expenses; so we presume a mine must have income of some sort out of which to claim these benefits. To put accounting principles on Section 83a would not suggest that you capitalize your exploration expenses.

MR.STEWART: Let me put it to you in another way. For corporate purposes, how would you treat this type of expenditure?

MR. DIX: For corporate purposes?

MR. STEWART: Yes?

MR. DIX: It would be charged as outside exploration. It would be charged right in the account. Some companies might charge it to surplus, but normally I think you will find it shown on your current revenue account.

MR. FOSTER: It depends on the particular case. If you are talking about prior, pre-production expenses, they are normally deferred for write-off purposes. If

you are taking in the costs subsequent to production, that is all operating expenses, and expenses normally against earned income.

MR. DIX: I am assuming that we have a defined difference between the two.

THE CHAIRMAN: Let us come back to our example. Let us take a brand new company starting into operation, which acquires a particular property, in respect of which it incurs exploration expense. Let us suppose it is fortunate and that it has got something there and proceeds with the development of that property. The property itself goes into production. How do you treat that for corporate purposes, the pre-production expense, in relation to that particular property?

MR. DIX: We have a gentleman here who is an expert on that.

MR. CORISTINE: The pre-production expense you are referring to -- that is, the accounting which normally is deferred as pre-production expense -- so the shareholders are aware that this amount is available for write-off in the income.

MR. STEWART: So, in effect, it is capitalized?

Let us remain with this particular company. It has this excess in connection with its first property. It then embarks on a further exploration program on some other property. Let us take the ideal situation where it is successful there as well. After having incurred certain exploration and development expenses, would the exploration and development expenses

on the second property not be treated for balance sheet purposes in the same way as those for the first?

MR. DIX: I think a lot depends there, Mr. Stewart, on the circumstances under which it incurs the expense of the new property. If it is entirely, wholly owned and it is found to be basic exploration, then it would be section 83a and in all probability would not be capitalized.

MR. STEWART: Excuse me, I am not talking about tax purposes, I am talking about the presentation of accounts for corporate or shareholders purposes.

MR. DIX: Normally, when we talk from a mining point of view, that is a company, that is income -- the company in the mining business that has an income -- normally we talk of section 83 as outside exploration expenses, which are current charges against revenue, under normal conditions. The only time we would say they are deferred or capitalized is in the event that corporation would incorporate a wholly owned subsidiary for the purpose of exploring and developing this second property. In those cases it is quite possible that company B might capitalize its exploration and development expenses.

MR. STEWART: I cannot profess to be an accountant, and in particular I cannot profess to be a mining accountant; but I am told that there is a book called "Mining Accounting in Canada" written by Messrs. Little and McDonald. I have no doubt many of you are quite familiar with it. I understand it indicates that expenses of the sort we are talking about, and I am

referring to exploration prospecting and development expenses, are often written off over an arbitrarily short period of time, such as four years, commencing with production. Now, would you comment on that?

MR. DIX: I think that reference is probably to old 4.5, in which exploration and development expenses are permitted to be written off. Tax-wise, you have influences of tax laws involving rates of write-off on accounting principles. That particular regulation provides 25 per cent per annum and that may be where the four year period comes in, but personally I do not think that is very significant in current accounting practice with regard to exploration and development. Again, I think Mr. Foster would have more knowledge than I on that particular question.

MR. FOSTER: This brings up the question raised before, as to normal accounting practice in write-off deferred development. I do not know what the normal accounting practice would be to write-off deferred development, because each one would be determined by the life of the mine, the amount of the ore and experience has proven that sometimes a long term life mine suddenly ceases, because of world markets, and that going into production with a very limited amount of reserves has sometimes proved to be extended greatly within a reasonably few years.

MR. ELLIOTT: Mr. Chairman, I would like to make a comment with regard to this. I think that perhaps there are two different aspects of this thing. One is capital of one company may very well be current expenses

in a normal mine accounting approach in another company. A mine that is a producing mine and is carrying on what we call outside exploration, is looking to perpetuating its. You have to take the limits of whatever the ore body might be. The only way it can extend or expand its life is to find new ore bodies. In the normal course of that, every industry tries to locate its raw materials wherever they may be. The mining industry has to find them. To that extent I think section 83a, as it is written here and as understood by us, exploration prospecting and developing expenses, refers primarily to that, and would, I think, in most accounting statements be set out or written off currently, as current expenses, unless with one possible exception, that during the year you turned up something that was obviously going to be a mine. Then it might suit your book to capitalize that, because for reasons peculiar to that particular situation.

On the other hand, a company that is incorporated, say to develop a prospect, and carries on a program of work, make surveys, carry out exploration, diamond drilling, or perhaps underground work. They would capitalize that. That is all capital. At least, they would defer it. It is not capital and has no value until it has produced an ore body out of which they can recover it, but it is a deferred cost of dealing with that mine, if ore proves to be there. I think that is the main distinction in approach being made here, in a company seeking to perpetuate its expenditure in finding the ore, regarding it as a current expense, and

its prime object at the moment is to develop the specific property, and it is a capital or deferred expenditure.

THE CHAIRMAN: Mr. Stewart, I am enjoying this discussion on accounting, and am glad to know about it, but I think perhaps that when you stress this, you might as well take an open suggestion and settle it as deferred. I must say it is very hard to draw a distinction between what is capital expenditure and which expenditures are deferred, and I do not think they try to do so.

MR. STEWART: Thank you Mr. Chairman.

Let us deal, then, with the case where a particular expenditure which can properly be regarded as exploration prospecting and development expenditure has been deferred.

Would it be correct to say that that deferred expenditure would ordinarily be recovered over the period of the useful life of the mine, whereas under section 83a it is permitted to be recovered as soon as the income from the mine permits?

MR. DIX: I can see. I think I understand that question, Mr. Stewart. Again, the mine that is deferring its expenditure in all probability has not got capital income out of which to make use of section 83a. Therefore, it is hardly a question as to whether it would otherwise have taken it under section 83. If it has deferred it, it has deferred it in all probability for the purpose of waiting until that particular property is in production and then recovering that

particular item on exploration. Whether a company is in a position to have a choice as to whether it claims under section 83 or whether it prefers to claim it later, depends on the nature of the particular company. If it is deferred, in all probability it is a new mine.

MR. STEWART: Let us assume for a moment that it is a new mine.

MR. DIX: If it is a new mine, then it is not section 83a.

MR. STEWART: I quite agree. I thought we had agreed earlier, Mr. Dix, that if we started off with a new company and it acquires a property, it proceeds to explore and develop that property, then the expense will ultimately be recoverable, or can ultimately be recovered, under section 83a. Is that not so?

THE CHAIRMAN: Not if my note is correct. It says that section 83a equals and is underlined outside exploration.

MR. STEWART: I then proceeded to give the example of a company which was just starting in with its first property and in that particular case there was a distinction; but we got into section 83a.

MR. DIX: Yes.

MR. STEWART: What I am now asking is this. In that particular case, which may be a very unusual type of case -- I am not sure -- in that particular case where this company proceeds to produce from that first property and it has certain preferred expenditure, as a matter of corporate accounting, were it not for section 83a, would that deferred expenditure be written

off over the period of the useful life of the mine?

MR. DIX: That is right: That would be the normal practice.

MR. STEWART: So the effect of Section 83a for tax purposes is to expedite or speed up the recovery of that expense for tax purposes?

MR. DIX: To the extent that there is income.

MR. FOSTER: May I ask what is the useful life of the mine. This is the problem where you attempt to determine the rate of write-off written, where it is capital development.

MR. STEWART: That I am sure is a very difficult question.

MR. FOSTER: It does not necessarily work according to plan.

MR. STEWART: What I am really getting at is this. In the particular type of case that we are discussing now, and dealing with this particular type of write-off, do we not find that section 83a serves one of the purposes, at any rate, which a depletion allowance may serve?

MR. EDMONSTONE: Mr. Stewart, I would say no, to this extent, permitting the early recovery of this money, this exploration money, it puts it back into circulation again much faster. This is part of the $45 million expenditure that the industry makes annually in finding new mines.

MR. STEWART: With that qualification, would you agree with my proposition?

MR. EDMONSTONE: This is an all-encompassing

qualification, as far as I am concerned.

MR. STEWART: Let me go on to try to compare this Canadian allowance with its American equivalent.

THE CHAIRMAN: Before you do, do you mind explaining to me, or to us, or have your witnesses do so, what is accomplished by Section 83a which would not otherwise be accomplished. The other thing I can say is that it does permit deduction currently of outside exploration. I would have thought all exploration other than that would have been deducted, if any, under section 83, and was deducted before there was section 83a. Am I not correct?

MR. DIX: That is correct, Mr. Chairman.

COMMISSIONER WALLS: Does Section 83 not cover all shaft work and under ground work and development, previous to coming into operation?

THE CHAIRMAN: But you do not need it for that.

My question was, what does it accomplish which is not otherwise accomplished. The only thing accomplished is outside work, because everything else would be achieved without that section in the Act.

MR. STEWART: Would it be achieved as normally?

THE CHAIRMAN: I think it would be achieved as normally.

MR. DIX: No.

COMMISSIONER PERRY: You mentioned the deduction currently of outside exploration ---

THE CHAIRMAN: I was incorrect.

COMMISSIONER PERRY: It is a question of the deduction period.

COMMISSIONER GRANT: Will you explain to me, on a site or shaft, the actual sinking of the shaft into the ground is a development expense, but the shaft house, the super structure above ground, would be capital expenditure. Is that right?

MR. DIX: That is correct.

COMMISSIONER GRANT: And all your underground would be development expenditure, taking up new ore bodies underground would be development expenditure, against expenditure in that one year. But it is prolonging the life of the mine. Is that expenditure ever capitalized? Is it optional in any way?

MR. DIX: I think you will find a varied method of treatment by companies. Here you are getting into class 12 shafts and other similar underground workings. You have main haulage ways. Those are your permitted capital cost allowances in the Act, to that extent from zero to 100 per cent, which in fact means that if you have income you can deduct all the cost of your shaft sinking in any particular taxation year.

The workings above ground, the head frame, the ship walls, the housing, all becomes permanent mine buildings, which are capital expenditures for which capital allowances are made in class 10. There is that distinction as between shaft and main haulage works and buildings above ground. I do not know whether that answers your question, Mr. Grant, or whether I have only just touched it in part.

COMMISSIONER GRANT: I can certainly see that

where you have anything put above the ground, it would fall into a capital expenditure, but I would also have thought that the very sinking of the shaft in a mine, the main shaft in that mine, would also be a capital expenditure.

MR. DIX: There may be many shafts on a mine. It could start out to be a prospect shaft. There are many prospect shafts. There may be fifteen on one main shaft. Then there are ventialting shafts which really are inverted shafts, which, let us say, go from the underground up to the surface. You could distinguish as between shafts that might be capitalized and shafts that might be charged off. I know some companies charge them off separately to their revenue account, to the extent that they are expenditures, even though perhaps they may not be able to claim it all for tax purposes. Other companies charge them to capital, the same as they do their drillings. I think perhaps you would find various methods, accounting-wise, in treating them.

COMMISSIONER GRANT: It certainly does not follow that expenditures underground are of a nature that can be written off against current income.

MR. DIX: I think the facts of that type of expenditure, its very nature, determine whether it could be written off either as current expenditures or as section 83a. Certainly, if it is outside, it is section 83a, even though it might be underground.

COMMISSIONER GRANT: In a coal mine you might have two or three miles of track rail, and the laying of the track, which would seem to be of a capital nature.

MR. DIX: Yes, one or two of the big problems involved in that sort of thing is in determining what is the main haulage way. In a mine one could have a number of main haulage ways, but for the purpose of administration of Class 12 there could be only one main haulage way or perhaps two, but not a series, even though it is more easily definable in a coal mine, where seams are long. In an extremely difficult low type of mining, you could have a series of main tramways or trapways or main haulage ways to a particulare ore body. It depends on the nature of the ore, how you are going to extract it, as to what is a main haulage way. In other words, which is the capital item and which do the departments say is current development expense. We have these problems but I do not think they are of a major nature with the industry.

THE CHAIRMAN: Mr. Stewart, I think I understand now that Section 83a brings in as a charge against income, outside exploration, which would not otherwise be so charged and also accelerates certain charges which would not be charged off in the year, which otherwise would be deferred. Is that correct?

MR. STEWART: That seems to be a fairly good summary of the situation, Mr. Chairman.

THE CHAIRMAN: Thank you.

MR. STEWART: We were going to come to the question of the corresponding position in the United States. Here I will attempt to indicate my understanding of the situation, so that you can correct me to the extent that it does not agree with yours. As I understand it,

in the United States, exploration and development expenditure may be either deducted within limits, which I will come to, or set up as deferred expenditure and deferred rateability as the deposit is exhausted.

So far as exploration expenditures are concerned, as I understand it, they are limited to $100,000.00 or a total of $400,000.00; for the purposes of current deduction. There is no similar limitation, that is, dollar limitation, as to development expenses. Is that a correct summation of the position?

MR. DIX: I think I will ask Mr. Coristine to comment on that, because I think that is only one-half of the problem.

MR. CORISTINE: That is right, Mr. Stewart, you are allowed up to $400.00.00 exploration and anything in excess of that you take back in capital cost depletion. With respect to that capital or expenses there is no exemption.

MR. STEWART: If that is so, I take it that the Canadian rules with regard to this type of expense are at least as liberal as the American rules. Do you agree with that?

MR. CORISTINE: I think so, sir, yes.

MR. STEWART: Mr. Dix has referred to section 83a, but leaving that aside for the moment, has your industry any major problems under the present provisions of section 83a?

MR. DIX: Major administration problems?

MR. STEWART: Yes?

MR. DIX: Or major industrial problems, or both?

MR. STEWART: Let us take one at a time. Have you an administration problem?

MR. DIX: As far as I am concerned I do not think the industry has any major administration problem with regard to section 83a.

MR. STEWART: And that extends to the administration by the Department?

MR. DIX: Do we all agree on that?

(Silence).

MR. STEWART: Does it cause your industry any concern that when section 83a was amended in 1962 to enable the petroleum industry to deduct land acquisition costs of certain types, this extension was confined to the petroleum industry and did not extend to the mining industry?

MR. DIX: That is correct.

MR. STEWART: Did it cause you some concern?

MR. DIX: No, it did not cause us any concern.

MR. STEWART: I observe that in your submission you indicate that the Canadian Metal Mining Association has, I think, 95 members atthe present time. It is indicated that those members represent about 95 per cent of the mining production in Canada at the moment.

By the same token, in the brief, that of the Mining Association of British Columbia, there are approximately 53 members listed, but as they are broadly representative, I take it of the industry, of the producers at any rate in that province.

Now, having regard to the figures you have given for mining production in Canada, both in your

submission and in your remarks this morning, it would appear that on the average your members are very substantial producers, if we are talking about the production of two or three thousand million dollars, divided among 100 companies, the average amount is quite large. So that the next question I was going to put to you may not be too material, but it is this. Does section 83a tend to favour the large operator as opposed to the small operator, having regard to this, that the large operator presumably has income from a number of sources and therefore can set his off propery exploration off against other income, whereas the small operator would not be in that happy position. Could you comment for us on that?

MR. DIX: Well, Mr. Stewart, I think that is a question of relativety. What is large for one might be small for another. What might be a substantial sum for a small company might be a very small sun for a large company like International Nickel. It is a question of relativity. It is a question whether we favour large companies. I do not think there is any favouritism in Section 83a with regard to large companies, because again we are looking at a few of the companies. Section 83 gives the same interest to any company that is in the business of mining or exploring for minerals. There are in fact many companies that never actually get into the production stage, which can use Section 83a. One must look at the whole industry as a group. I do not think that you can find that there is any favouritism to the large operator.

A large operator will probably spend more on outside exploration than the other, but again it will be somewhat relative.

Again, I do not think that the size of the budget for outside exploration has any bearing on the rate of reward for that particular company. The risks involved and the elements of hazard in finding new mines are so high that one cannot plot a curve by saying that if you spend $1 million you are going to find twice as many mines, as you would if you spent half a million dollars. That does not work in the mining industry. It depends on your program, where you are going to spend it and what you can afford to spend.

Some companies spend a greater proportion of their income than others. In all cases, Section 83a works with equality amongst all companies in the business of mining or exploring for minerals.

MR. STEWART: I realize that Section 83 is a rule of general application and applies to anybody in your particular business. There are certain provisions we are talking about which are open to anyone whose principle business is mining or exploring for minerals, that is, every corporation.

You made one remark in your last statement, Mr. Dix. I might have misunderstood it, but it stuck in my mind. I think you said that a company which had no production will still have the benefit of Section 83a, and I just cannot help wondering how that could be. Does Section 83a not depend on having income?

MR. DIX: Normally I think it would, but you may

have an isolated case. A company might be in the business and might be an exploration company.

MR. STEWART: But if it is an exploration company, unless it has investment ---

MR. DIX: Certainly, to make any use of Section 83a you must have income from some source.

MR. STEWART: In any event, if these 95 companies of your product 95 per cent of this two or three thousand million dollars of production, they are basically or on the average substantial companies. It does seem to me that -- let me put it this way -- I can well understand that this allowance, or these provisions, are of great importance to them and that they may have the effect of encouraging additional exploration. I would come back to my question.

Is this provision one which benefits the large corporation of that sort and which is really of limited importance to the small concern which is just attempting to get started?

MR. WANSBROUGH: Are there comments on that?

MR. DIX: I think I have commented. Perhaps other members of the delegation would wish to comment also.

MR. MITCHELL: I think we have had a lot of experience of this in British Columbia. Many of the companies which are members of the Canadian Metal Mines Association are, by reason of the activities in British Columbia, also members of the Mine Association in British Columbia. But there are quite a number of smaller operators in the province, and it would be easy

to observe from several of the balance sheets, that the investment return in some of those companies plays quite a distinct part in the activities. They get a distinct benefit. Because of the fluctuation of metal markets, they may not make any money this year. They probably have got other income which is perhaps even of disproportionate significance to them.

MR. STEWART: Would there not be cases where people start off with limited resources, where they utilize those resources to the hilt in getting a particular property into production, granted that once they do bring it into production, once the three-year period is over, they can utilize Section 83a; but may it not be a considerable period before their financial position will be such as to permit them to engage in off-property exploration?

MR. MITCHELL: Yes.

MR. STEWART: Theoretically, section 83a is available to them. It may be difficult and it may take a long time for the new small enterprise to be able to make real use of it.

MR. MITCHELL: Yes. In certain cases that would be true. Some of these smaller properties may by their physical nature be probably more active in finding and bringing into production other small properties, than the larger ones are. That is to say, a property with only 500,00 tons might not be of any particular interest to one of the larger companies represented here. Quite often, in our experience, the larger companies will turn over the results of the

preliminary prospecting, if you like, and exploration, to a smaller company and say "This is too small for us but if you like to go ahead with it, that is fine" -- and I have seen that done on a gratis basis. Then the smaller company which is perhaps more suited because it has a smaller staff and a smaller organization, will proceed from there.

MR. BRADFIELD: The small company might be in an area geographically familiar with the place and has the advantage over a large company which has not been operating in that district, and of course the big element is luck.

MR. ELLIOTT: I should say your proposition is correct. If a company has no taxable income, that is, expending capital funds, or tax free funds, dividends from other Canadian companies, it cannot realize any benefit directly under this. But it does realize it in that it is attractive to those companies, because of a certain element of protection, plus the fact that if they do have some modest fortune they will eventually realize under them.

THE CHAIRMAN: Mr. Stewart, I was going to hold my comment until you got through, but it seems to me it would shorten the discussion if I make it here.

Rather than the discrimination being between large and small, it seems to me, and I thought it was said, that there is a distinction between those with income and those with prospective income under section 83a. Certainly if you have income now you are at an advantage over one with a prospective income. The only

way that can be brought into balance as between the two is if section 83a expenses were deductible from the property on which it is being spent, because then in both cases it would relate to prospective income and not, as I say, in one case to income and in the other case to prospective income.

However, that is not the purpose of Section 83a, according to my belief, so I suppose you are left with being out of balance, as I think it is.

MR. DIX: I think Mr. Chairman a brief review of the history in section 83a perhaps might give a clue to this. Before the war a mining company, a company in the business of mining or exploring for minerals in Canada had no allowance for its outside exploration. I should like to call it "outside" because I think it means what it says -- away from the main property.

The mining industry of course has different eras in Canada. Particularly looking to our own province, we had the mining of silver in 1903 in Cobalt and the development of the silver mines in that area. That formed a basis to a great extent for the continued exploration and development of the mining industry in the province. The technalities of Cobalt and the mining knowledge developed there has been spread to Porcupine, Gordon Lake and the Noranda area. These were out-comings of a very rugged group of mining entrepreneurs. The necessity for allowances for what you might call outside exploration could in those days really easily have been related to the smallness of the rate of taxation. In other words,they were not in effect major

problems. There were plenty of sources of risk capital. It is true that a lot of it came from Britain in the early days and a lot come from the United States, particularly in Cobalt.

Then, with the depression years, of course exploration fell completely flat on its face in Canada, particularly in Ontario. There was very little to encourage anybody to go into mining.

Of course the same is true for many other industries. There was no profit in them.

The introduction of the vital need for metals during the war years made it paramount that something must be done. The industry did this of its own accord.

First of all came the big demand for gold production of 1940, which developed into the greatest production and the greatest increase in gold production, because the first thing we needed to win the war was that necessary type of funds needed for buying our guns and buying them in the countries in which we were. As you know, it played a very important part in Normandy, through the gold production of Canada.

Then there was the question of strategic minerals. We were getting into a different age altogether. The first introduction to outside exploration gave mining companies an allowance for strategic minerals. It was a very nominal sum, I think, in the initial instance, only $4,000.00 or $5,000.00 a year. I am not sure. This was later extended to include a deduction from tax, equivalent to a percentage in relation to the amount of money spent on outside

exploration, not only for strategic minerals but for certain other minerals.

It was then later extended to all minerals, and more recently of course has come in as section 83, which is a general allowance now for exploration.

This undoubtedly has been of great benefit to us in building Canada's mineral industry to the stage in which it is today. It is also very important to consider it as a useful vehicle for maintaining its industry and perhaps encouraging it to make further progress, because as soon as you take a ton of ore out of the ground, that is a ton less. These mines all have their limits of life and it would seem to me that section 83 has performed a very valuable function, when you look at the history of this allowance in our Canadian tax scheme. It is certainly now part of our business to explore the mine.

THE CHAIRMAN: Thank you, Mr. Dix.

MR. STEWART: Now we have been talking so far about companies whose principle business is mining or exploring for minerals. Mr. Wansbrough, are your members essentially in that category?

MR. WANSBROUGH: Yes, and the eligibility for membership in the Association is that you have to be a producer mine or operating, or an active exploration company.

MR. STEWART: So when we come to other classifications I am sure you can indicate what the position is. But your members may not come within them.

I should like to come first to a classification

of companies whose principle business is not mining or exploration for minerals but which operate certain mines and which are entitled to write-off pre-production expense under regulation 1205 as I understand it.

Could you tell me whether this is a substantial group of people? Does this regulation 1205 apply to a large number of people?

MR. DIX: Speaking personally, Mr. Stewart, it must be so small that I cannot put my finger of a single. There could be; but as far as I am concerned section 83 is being used by companies whose principle business is mining or exploring for minerals. I do not know of any other group that has taken advantage of it. Some other member of the delegation may know of some unusual circumstances.

MR. FOSTER: There may be some mines now closed down who were under regulation 1205. They were prior to 1952, and if some day they become reactivated, section 1205 would bring them forward.

MR. STEWART: I see. Then there is one subsection of Section 83a which applies to another group of companies, those whose principle business is not mining or exploration for minerals but whose principle business is production or marketing of sodium chlorate, or potash, or whose business includes manufacturing products, the manufacturing of which involves a manufacturing process of sodium chlorate or potash. Is that a substantial group of taxpayers?

MR. DIX: A new group?

MR. WANSBROUGH: Potash. We have one man on the

list whose main thing is to mine potash in Saskatchewan. I am not exactly sure of the position of other potash companies. There are some others beginning or about to begin but I am afraid we have not got anyone here who can speak for them.

MR. STEWART: Then there is a further group of companies whose principle business is not mining or exploring for minerals but which operate industrial mineral mines which are contained in bedded deposits. As I understand it, section 83 does not extent to that group but they in fact can recover their pre-production expense under schedule E of the regulations, which permits these expenditures to be written off in effect over the life of the industrial mineral mine. Would that be in accordance with your understanding of the situation?

MR. DIX: Yes.

MR. STEWART: When we talk about bedded deposits, are we thinking of all bedeed deposits or are we thinking of clay, gravel, gypsum, potash and sand. Are these the main ones?

MR. DIX: Yes, those are the main ones, that type of mineral.

MR. STEWART: You raise in your brief the question of extending section 83a so that it would apply to exploration expenditures outside Canada. That is on page 15.

COMMISSIONER WALLS: I would like to ask a question about regulation 1205.

I was rather surprised to hear you say you

know of anybody who comes under 1205. Surely there are a lot of mining syndicates -- surely there are many of these mining syndicates, as I have heard of many of them.

The thing that concerns me is that they come under 1205 and their pre-production expense, as I understand it, can be written of at a rate not exceeding 25 per cent. They have this big advantage over section 83a, in that they are in no way tied to their income and that they can hold the write-off until any future years that it suits their purpose to claim it. It seems to me that this is of sufficient advantage to these syndicates.

MR.DIX: Mr. Walls, the mining industry certainly, is itself making greater use of the syndicate type of operation. The modern methods of exploration, particularly geophysical types of exploration, are such as to make the cost tremendous in relation to what we normally used to face as the normal cost of exploration. Therefore, it is seldom advisable for a large company to go this thing alone.

In each case they form partnerships, you might say, with other mining groups. They might be mining companies, they might be mining syndicates, or they might be mining companies whose business is just to explore for minerals. This is quite a common method today of exploring for mines. That is because of the very nature of the exploration. If it is air borne work, it is very expensive and very often one particular company has a particular knowledge which it can add to the partnership, whereas the other might have knowledge

of markets which it can add to the partnership. This is very often the way it is done. I cannot answer your question specifically with regard to 1205 because, as I said, I have very little knowledge of companies which are making use of this particular regulation. If you talk to the National Revenue Department, they infer that Section 83a has to some extent taken the place of 1205. Regulation 1205 is a very old regulation. Some other member here might have knowledge of 1205 but I cannot help you in the question, because I do not know of anybody.

COMMISSIONER WALLS: Would it not be advantageous in terms of Section 83a if you could postpone exploration exemption to the years you wanted to postpone it to, in certain circumstances.

MR. DIX: Yes, I would agree but under the conditions you mention to me it would seem that the syndicate could take advantage of this for tax.

MR. STEWART: I am just continuing with the point which Mr. Walls has raised. Is Section 1205 of the Regulations available not only to syndicates but to corporations or individuals or partnerships who do engage in exploration, who do achieve production but who cannot bring themselves within the mining provisions of section 83a?

MR. DIX: If that position exists, I do not think it is of major importance, if we consider that it has hardly been used by these particular companies.

Your question was long and I may not have got all your points.

MR. STEWART: I am sorry for the length but I find it sometimes hard to link these points.

If we look at subsection (4) of Section 83a, this relates simply to the petroleum industry. It applies to associations, partnerships or syndicates. Sub-section 4a also is in the same category. It simply applies to a different period from sub-section 4. Then if we get to 4b, and we find that it relates to corporations, apart from those whose principal business is one of the two types, but that it again relates to petroleum income, as opposed to mining income.

Then, in 4c, we are dealing with individuals, but it is a straight petroleum section or provision. Therefore, so far as individuals, partnerships, associations and syndicates are concerned, if there is any relief at all in respect of this type of expenditure it appears that it must come under section 1205.

MR. DIX: That is right.

COMMISSIONER GRANT: Does Section 1205 mean that the taxpayer could deduct his expenses from other income?

MR. STEWART: I would have thought so, Mr. Grant, because let us see that Section 1205.01 permits a deduction in compution of income.

COMMISSIONER GRANT: I was under the impression that was not permitted, or perhaps it is limited to exploration expense for an individual.

MR. STEWART: The words "may deduct in computing his income", Mr. Grant, are general.

COMMISSIONER GRANT: It should be all embracing.

MR. STEWART: A quick look at the other provisions of the regulation -- I do not see any qualifications.

COMMISSIONER GRANT: Section 83a of course is restricted to the income of a corporation in so far as it is --

MR. STEWART: Section 83a refers to companies whose principle business is mining or exploring.

MR. DIX: The condition in 1205 is, is it not, that the taxpayer may operate the mine.

MR. STEWART: That is correct.

MR. DIX: So to that extent he is a mine operator. He may not be a mine operation.

MR. STEWART: That concludes my questions under Section 83a.

THE CHAIRMAN: What are the other sections?

MR. STEWART: Capital cost allowances; depletion; followed, to the extent that time permits, with some other points.

THE CHAIRMAN: I will see if there are any further questions on Section 83a.

MR. WANSBROUGH: May I make one comment. It seems to me that Mr. Stewart's questions were directed at one point, which was not followed up, and he may wish to follow it up. There was a question in regard to explorations outside Canada. That was not followed up.

MR. STEWART: That is quite right. I am afraid I was sidetracked on that. I forget how it happened.

You did make this point on page 15 of your brief. I think Mr. Bradfield also mentioned that ther e is this restriction under our present regulations. You indicate on page 15 that a number of Canadian companies are now engaged on mining exploration and development and mining. Is this being done through branches or subsidiaries?

THE CHAIRMAN: Just a moment Mr. Stewart. You referred to restrictions. I think we are only dealing with the lack of incentives. There are no concessions given to foreign exploration. That is all we are concerned with here.

MR. DIX: The restriction in Section 83a is only limited to expenditures in Canada.

MR. WANSBROUGH: Whereas the provisions in the United States to which Mr. Stewart referred are not confined to exploration activities within the United States.

THE CHAIRMAN: Therefore, the point is that Section 83a is inoperative with regard to exploration outside Canada and as such exploration outside Canada would not be deductible at all. Is that right? It would not be deductible from Canadian income, it would be deductible if the exploration resulted in income outside of Canada. Presumably it depends on the country.

MR. STEWART: In fact, one of these Canadian interests are engaged in this interest outside of Canada. Do they do it through branches or subsidiaries.

MR. BRADFIELD: I think we have property in

Chile, for example, going into operation any day. It is a small copper mine. I think this has been a good thing for Canada but it has nothing to do with taxes. It does enable us to give the men some experinece in other countries. They are also able to purchase a lot of equipment and supplies in Canada for export, to be utilized in this property.

I think that if we had some encouragement outside we could at times make use of new prospecting methods that we may have jumped on some other people on.

It is a great thing for our young men if they are able to have Canadians exploit and develop mines in other countries, giving us a wider scope for youngsters to get into the minerals profession in Canada.

At one time the Canadian mining engineers were favourably known all over the world. Today that is not the case. We are trying to rectify that and this will be a great help, if more companies were encouraged to send men abroad to explore and develop new mines.

MR. STEWART: May I ask Mr. Bradfield if in this Chilean case he mentions, -- you are operating there a branch of a Canadian company or through a local company?

MR. BRADFIELD: It is another company, in that instance, we have as a partner a Nicaraguan company which is another subsidiary of ours.

MR. STEWART: Would you find in the Latin American companies, by and large, there is any legislation which requires the formation of local companies to exploit natural resources?

MR. BRADFIELD: Not in Chile.

MR. STEWART: Would there be some of the Latin American countries?

MR. BRADFIELD: Yes, in some. Mexico.

MR. STEWART: If you do incur exploration abroad through a branch of a Canadian company, I take it that the chances are that that particular country will permit you for its tax purposes to deduct your exploration and development expenditure?

MR. BRADFIELD: Not in every case, as far as I know. I am afraid I am not competent to answer that. They certainly do in Australia.

MR. STEWART: In any event, what you would like to be permitted to do is off-set expenditure of this sort, incurred in foreign countries, against Canadian income?

MR. BRADFIELD: I think it would be a good thing for Canada.

THE CHAIRMAN: Mr. Stewart then gets down to incentives to encourage opening upon a broader basis.

MR. STEWART: That is right.

THE CHAIRMAN: We are concerned with the national economy first of all, and the national economy is primarily concerned at the moment with employment in Canada. You, Mr. Bradfield, say you have successful explorations in Chile, or wherever else they may be, but they do not in any way replace what would otherwise be Canadian employment in Canadian mines.

MR. BRADFIELD: No, I think the only hope with regard to employment is that it encourages more

people to come into the industry and if we can sell or purchase some equipment or supplies in Canada and direct them to these other countries, things that are not available there, it helps in employment. If you do spend money, and you spend it in Chile and if it develops Canada, the mine in Canada is as good, and it might be better, for Canadian economy.

MR. ROW: Without this allowance of this expenditure, we Canadians find ourselves at terrific disadvantage in competing with others in those foreign mining fields. While I realize that Canadians are concerned with creating employment at home, on the other hand there are efforts there through which we contribute, through United Nations, to develop these mineral resources in so-called underdeveloped countries. I would put forth the thought that you are better developed under agencies of private enterprise than possibly under agencies of the United Nations.

THE CHAIRMAN: Yes, but Mr. Row, the question is not whether or not you are fairly taxed, it is a question whether or not the Canadian laws let you off some measure which would be normally taxed, in order to encourage you to go abroad and develop. It seems to me that whereas it may be an excellent idea to encourage development in Canada by taking some of the tax load off and putting it onto somebody else, it is more difficult argument to make that point with regard to development outside of Canada.

MR. ROW: We are faced with the situation of a crown corporation. The crown corporation is going into

a new front.

THE CHAIRMAN: That, I think, is another point.

COMMISSIONER WALLS: I take it that you want to create a mining Colombo Plan.

MR. WANSBROUGH: You have brought us back quite correctly to the fundamental consideration of employment. There is another one -- foreign exchange. One of the significant results of the kind of thing you are suggesting here might very well be the beneficial effect in terms of foreign exchange.

THE CHAIRMAN: It could well be.

MR. STEWART: Now, Mr. Chairman, if I could move to the question of capital cost allowances. I think it is the fact, gentlemen, that at the present time mining, buildings, apart from office buildings and refineries, mining machinery and equipment, are taxed under class 10 for capital cost allowance purposes, under which the rate is 30 per cent.

MR. DIX: That is correct.

MR. STEWART: As I understand it, the normal rates of depreciation on buildings, apart from mining buildings, are let us say five to 10 per cent depending on the type of construction and the normal rate on machinery and equipment is, I think, 20 per cent.

Could you explin why it is that mining buildings, machinery and equipment should be entitled to a more favourable rate for capital cost allowance purposes.

MR. DIX: Mr. Stewart, the rate of capital cost allowance for mining buildings, machinery and

equipment, in class 12, develops from the fact that the normal average tax paying life of a mine is a very short period of time.

Some years ago when the well known Mutch report indicated that the average tax paying life of a mine in the province of Ontario was something less than eight years. It is true that there are well established and long established mining companies in Canada that have been in existence for a lot more than eight years and have been paying taxes for more than eight years but to take the industry as a whole and that is not just looking at a few successful mines but looking at the industry as a whole, then 30 per cent on the diminishing balance, which is, let us say, very similar to 15 per cent straight line, does not seem at all out of line with regard to the normal spending life of a mine in Canada.

MR. STEWART: When you say that 30 per cent diminishing is equivalent to 15 per cent straight line, I suppose it depends on the period you are thinking of; but as I understand it 30 per cent on diminishing balance involves writing off two-thirds in the first three years.

MR. DIX: Yes. You will get it sooner, if you go on diminishing balance, by straight line, but in the second year period, during which normally you would have it off in the straight line, you have practically got it written off, under the diminishing balance, except that you always have a residue which adds on.

MR. STEWART: What you are suggesting is that

we should treat mining buildings in the same category as some other type, which is entitled to 15 per cent straight line.

MR. DIX: I do not follow you there. Probably I was only half listening, as I was thinking of the next point.

MR. STEWART: We are dealing with two types of things, dealing with mining buildings, we are dealing with mining machinery and equipment. The normal rate under the capital cost allowances on buildings is not 15, it is 5 or 10; and the straight line would be approximately half of that again, say it might be 2½ and 5. Are you using 15 per cent because this is a straight line rate which permits complete recovery over a period of several years.

Just exploring this further, we have a three year period of exemption during which you need take no capital cost allowance at all. Then we have three more years in which 30 per cent you can write off two-thirds if you take the full allowance. On that basis I suppose that at the end of eight years if you have been in a position to take the full 30 per cent, the assets are pretty well completely written off for capital cost allowance purposes.

MR. DIX: For a new mine.

MR. STEWART: When you say "for a new mine" are you referring now to the fact that if there are a number of mines you will have assets of the same class which may not all be written off? I am not sure what the significance of the words "for a new mine" is.

MR. DIX: The significance is that if you apply it, it only applies to a new mine -- it could not mean that it applies to the mine in question.

MR. STEWART: Would it be the case that so far as your industry is concerned, recapture of depreciation is not a practical problem.

MR. DIX: I think that is a true statement. I might add that in a mining operation there is something peculiar about buildings and machiney in a mine. The mine usually is built in the bush, to start with. It eventually might become a town. But when that mine ceases its activity, when its work is done, unlike any other business, those buildings and equipment are for all intense and purposes useless. There is very little salvage value in a mine when it shuts down. I think all of us here have had practical experience in trying to dispose of plant after a mine has been shut down. Usually, the transportation charges alone do not warrant the removal, or let them be used for something else.

MR. STEWART: So that if you were not the recipients of this special rate under class 10, if you were taxed at the normal rate applicable, or if you were in a class with other buildings and with other machinery and equipment, at what appeared to be the more normal rates, if in a particular case you had a relatively short life for capital cost allowance purposes, such as eight years, then you presumably would get a terminal loss at the end of the period; because those assets would realize at most their salvage value, which is

apparently pretty minimal. I am not too clear why these particular assets are in class 10, as opposed to a class where the rate is lower. The fact that the property may have a limited life does seem to be a conclusive reason.

MR. DIX: Of course, if you are going to start a new mine, unlike any other business you cannot foresee, you cannot look into the ground. You can drill and get certain information, but even as in the case we could describe many situations where drilling has indicated an ore body and the ore body has been found to be something different.

Once you get down underground and get drifts out and take a look at it, if at the beginning one can say "Here is a profitable mine which is going to last twenty years" in those cases one could assume that the normal 5 per cent rate of depreciation or capital cost allowance might be something you could do. But you cannot see that in a mine. Even if you can, the economics, even if you could see, you do not know what the price of metals is going to be or what the economics of that operation are going to be for that length of time. When it is there, you cannot devote it to some other type of business.

MR. STEWART: So what you are saying in effect is that in this particular type of operation, even if you have taken the gamble of acquiring depreciable assets, the uncertainties inherrent in a mining operation are such that we should proceed on the basis that the useful life is going to be relatively short.

MR. DIX: I think the history of mining in Canada certain shows that.

MR. EDMONSTONE: Many of us in the industry ought to be able to pick his own rate of depreciation. The new depreciation regulations in the United States at present are having a tremendously good economic impact on that country.

MR. STEWART: I appreciate what you say, Mr. Edmonstone, about the new United States guide lines and the alternative system of permitting you to write your own ticket. I am not in any way suggesting that these things should not be considered here. I was trying to get to the apparent distinction between your industry and others which have the same type of asset.

THE CHAIRMAN: It is after 1:00 o'clock. Do you wish to continue?

MR. STEWART: I am in your hands.

THE CHAIRMAN: I would prefer to come back after lunch. However, gentlemen, we do not wish to delay you.

MR. WANSBROUGH: Mr. Chairman, we think we would like to come back, as there is more to be said.

---The Commission adjourned for lunch.

--- On resuming at 2.00 p.m.

THE CHAIRMAN: Mr. Stewart, I think you might proceed.

MR. STEWART: Thank you, Mr. Chairman. Gentlemen, I have a couple of questions with regard to the specific points you raise on page 16 (submission on behalf of the Canadian Metal Mining Association) with regard to capital cost allowances. You suggest, first of all, a change in the wording of Class 10. Could you tell us a little more about the significance of that suggested change?

MR. WANSBROUGH: Might I just say that some of these vacant seats will be filled. We have dedicated athletes among us who are working. However, in their absence I am sure Mr. Elliott will be happy to answer that question.

MR. ELLIOTT: I think the purpose of this is to clarify the wording of the section by including in it all the plant one frequently finds in a mine rather than the present wording which is capable of narrow interpretation. It is to administer correction rather than to bring in any new principles. The way in which the section is written presently does lead to considerable difference of opinion between the industry and the tax department in reference to what constitutes depreciable assets applicable for topical cost allowance.

MR. STEWART: Can you give us a few

examples of what the Department is not presently allowing under Class 10 which you would like to see included? I notice you have added the word "structures" and the words "associated facilities". Just what type of thing have you in mind?

MR. WANSBROUGH: I can think of one or two instances. Railway sidings are one; docks are another -- that kind of thing. Mr. Foster is here now and I think he would be able to say something about this.

We are being asked why the change is suggested on page 16 to include structures in Class 10, and associated facilities.

MR. DIX: Please excuse us, Mr. Chairman. We find taxis a little hard to come by in this town.

THE CHAIRMAN: We are referring to page 16 of the submission dealing with Class 10. Mr. Stewart has just inquired what would you attain by putting (g) and (k) together which is not now attained in the schedule.

MR. STEWART: And by adding the additional words suggested.

MR. FOSTER: Basically it is because the words which are now in the section are very limiting. There are such things as structures, buildings and machinery which are hard to define, things of this nature. Are they buildings? Are they pieces of machinery? We think as a unit it should be combined together to be all-encompassing.

MR. STEWART: We have railways sidings,

docks, etc. Are there any other major instances?

MR. FOSTER: I do not know of anything. Does anyone else have any problem on this?

MR. CORISTINE: As a practical matter, I think this amendment is intended to cover the assets that already are included in Class 10. but the previous wording was not sufficiently encompassing to cover it.

MR. STEWART: Moving on to Class 12, you want the word "underground" deleted. I remind the commissioners that Class 12 is a 100% deduction. I gather from the brief of the British Columbia Association that one of the reasons for suggesting the deletion of this particular word is that the present wording discriminates or may discriminate against the surface or open pit mining. Is there any other purpose in suggesting the change?

MR. DIX: I do not think so, Mr. Stewart. The reference to Class 12, of course, goes back to the days when open pit mining was no the common thing in Canadian mining. The shaft or the main haulageway normally could only exist underground. However, as indicated, particularly with the iron ore industry, you can have main haulageways which are not underground. While I do not think there have been any distinct administrative difficulties with regard to the determination of various expenditures as between surface and underground, there is a delicate area, perhaps, where the elimination of the word "underground" would more properly describe the intent of Class 12 for mine

shafts and main haulageways.

MR. STEWART: What is the treatment of roads -- and I am speaking about service roads -- for tax purposes?

MR. DIX: In our type of mining, of course, a road is a capital asset. I do not know what it is in the iron ore business. If it benefits hauling the ore, it could be a main haulageway.

MR. CORISTINE: If the road is permanent in nature and is to serve a number of properties, it would become Class 10, I think, as a mining asset. If it were just a temporary road to serve a property with a limited life, it might be charged off as development.

MR. STEWART: Would the effect of your proposed change in Class 12 be to permit you to charge a permanent road as, in effect, a current expense? Let us say you cannot take them at 100%.

MR. DIX: I do not think that is the intention.

MR. WANSBROUGH: That is not the purpose.

MR. DIX: That is not the purpose of our suggestion.

MR. ELLIOTT: The purpose of deferring the main shaft, main haulageways and similar underground work in the case of an underground mine as far as the Income Tax Act is concerned is to permit it to capitalise or defer those items and wipe them off in accordance with this provision. A similar right is not given to an open pit mine because of the fact that aboutthe only thing for a continuing use would be main haulageways, and

within the pit they are not recognized as roads. I think that is correct. Removal of the word "underground" would serve to bring that inequity into balance.

MR. STEWART: Mr. Chairman, I think I would like to move on, if you have no further questions on capital cost allowances, to the subject of depletion.

THE CHAIRMAN: Has any member any further questions in connection with capital cost allowances?

Go ahead, Mr. Stewart.

MR. STEWART: Gentlemen, dealing with the type of mine with which you are concerned, I take it the basic provisions we have to take into account are section 11(1)(b) of the Income Tax Act and section 1201 of the regulations. Is that the case?

MR. DIX: Part XII of the regulations? There are a number of other regulations.

MR. STEWART: Right. Under Part XII or under section 1201 of the regulations at any rate, the deduction is 33 1/3% of the production income except in regard to gold, where there is a special formula established.

MR. DIX: Yes.

MR. WANSBROUGH: That is right.

MR. DIX: It is 40% of mineral profits for gold or $4 per ounce.

MR. STEWART: Is there any feeling in your industry that depletion should not be computed on the present basis, which I understand is an overall corporate basis, but that we should switch to depletion

on a mine-by-mine basis?

MR. DIX: Mr. Stewart, the depletion regulations, insofar as the industry is concerned, have worked well throughout the history of mining in Ontario, Quebec and other provinces where we have mining operations. I do not think the industry has anything to suggest other than that the regulations have worked well. I think the proof is in the pudding there. We have a very substantial mining industry which has grown in Canada.

MR. STEWART: I cannot help comparing the representations you people have made on this subject of depletion with the representations some of the petroleum people have made. They do differ, as you may or may not know, in a number of respects of which this is one. They would much prefer to have depletion on a well-by-well, property-by-property basis. You do not seem to be making this point.

MR. DIX: No, I think basically the reason we do not join with the oil people in their suggestions is that depletion regulations are a basis of common knowledge as far as the mining industry is concerned. Everybody in the industry, and the investors in the industry, pretty well know what are the allowances for mining companies. We can see no reason why these things should be disturbed, as far as the mining industry is concerned in any event, it is pretty basic in our industry.

MR. STEWART: Then there is another point on which you seem to differ from the petroleum

industry as well. They have raised the question whether in the computation of production income it is appropriate to provide that section 83(a) expense must be deducted. I observe that you have raised this question with regard to shareholders deplection but not with regard to depletion of the company itself. Could you perhaps comment on that, or is the answer here again that you have had this rule for some time, that everybody in the industry understands it and is content to go along with it?

MR. DIX: We certainly understand these depletion regulations. As I say, they are quite simple to understand and we all know what they mean. I cannot see personally what advantage there would be to the mining industry in suggesting that they be changed. In other words, we have a system that has worked. Therefore, why disturb something that certainly has worked throughout the history of mining in this country?

MR. STEWART: You do not consider that the fact that section 83(a) expense must be deducted under regulation 1201 deters exploration effort?

MR. DIX: Your question, then, relates to why perhaps we do not suggest that section 83(a) expenses be eliminated before calculation for percentage depletion under the Income Tax Act? I presume that is the gist of your question.

MR. STEWART: I do not suggest that section 83(a) expenses be eliminated.

MR. DIX: No -- eliminated from the calaculation.

MR. STEWART: Eliminated from the calculation, yes.

MR. DIX: Yes. I do not think we have any particular reasons for not suggesting it. Perhaps you have put words into our mouths. Perhaps we much prefer to have our depletion allowances calculated before our deduction of exploration expenditures. But again, as far as depletion was concerned, we felt that here is a system that has worked well and we could not see any reason for change, except in one or two isolated instances -- and that is in regard to the one you mentioned about the shareholders where there has been no depletion simply because of a tax loss. We thought that was an inequity and we made that suggestion. We do not subscribe to any changes in a system, however, which seems to have been very effective.

MR. STEWART: I suppose it might be put in this way, that overall the incentives to continued exploration which we have under our tax system at the moment are sufficient to encourage your industry to go on exploring?

MR. DIX: They seem to be quite satisfactory. There is a basic difference between our industry and the oil industry in the relationship between the amount of money expended on exploration and the income. The amounts spent on oil exploration are very major in relation to the income in any particular situation. The oil industry has complained that by taking the exploration off and working on percentage depletion, in fact they are getting no

depletion because the more they spend the less they get.

MR. STEWART: This is the point they have been putting to us quite forcefully. In your case, the amount expended on exploration generally is a lower proportion of what you may expect to recover than in the case of the petroleum industry?

MR. DIX: It is a slower rate of recovery. In the oil industry, they must spend in relation to certain rights which they would otherwise lose.

MR. STEWART: There does not seem to be any suggestion in your submission that the American system of depletion is preferable to the Canadian system.

MR. DIX: We do not know too much about the American system. We can speak for our Canadian system and we are quite firmly convinced that our system has worked. Whether we would be more favoured by using American principles here, I do not know.

MR. STEWART: I know very little about the American system, but I would like for purposes of the record -- and to see if Mr. Coristine or someone else can comment -- to state my understanding of it, which is this. Under the American system you have two alternatives. You can take on the one hand cost depletion on a unit of production basis, or on the other hand you can take a percentage of gross income. The percentage, I think, in the mining field there is from about 10% to 23%, depending upon the type of mineral, subject to the proviso that that particular percentage of gross income may not exceed 50% of the net income from

the property. Now, you take the lower of the two. Is that basically the American system?

MR. CORISTINE: Yes, Mr. Stewart. I think one basic difference, however, is that in determining depletion you only deduct expenses with respect to their properties. If you have outside development, you do not have to deduct it in arriving at the profit subject to depletion, and you can determine it by each property.

MR. STEWART: Yes, it is on a property-by-property basis. Now, having regard to what you were saying earlier, Mr. Coristine, about the American system, I would like to read an extract from the book I referred earlier today, Mining and Mineral Processing in Canada, which as I said was published in 1957. I am reading now from page 359, and I quote:

> "While Canadian depletion rates seem superficial and more generous than the American, the fact that the former are calculated on the basis of net income and the latter on that of gross, makes it doubtful over an extended period of time whether Canadian deductions would be very much different from those allowed in the United States."

I think I can stop the quotation there. Would you care to comment on that?

MR. CORISTINE: I believe the American system gives greater allowance because there

is so much more flexibility where you can calculate it by properties. As I said before, sometimes you will have a loss property and an overall loss on your operation yet a profit on several of the properties you have, and you can take depletion even though you have overall loss and you can increase your overall loss. I believe there is more flexibility under the American system, but again I think it would depend on the circumstances. You have to take each company and study it separately.

MR. STEWART: So that in any event, neither system is necessarily more liberal than the other? It may be that on one particular set of facts one may work out better from the taxpayer's point of view and the next might go the other way?

MR. CORISTINE: Yes. In our particular case, the allowances in the United States would be considerably more liberal.

MR. STEWART: When you say in your particular case, you are referring to your particular company?

MR. CORISTINE: Yes.

MR. STEWART: You dealt with the function which the depletion allowance is intended to serve, I think, on pages 9 and 10 of your submission. Does it come down to this, that your industry should be permitted to recover the cost of its investment over the life of a particular mine, that you consider this to be an extractive industry, and that many years may elapse between the time of exploration and the time

of production? At the top of page 10 you make four points and at the bottom of that page you suggest another one. When we really get down to it, is there more to it than that over the life of the mine you should be able to recover your investment?

MR. DIX: I think basically that is true, Mr. Stewart. I think the importance of depletion is an industry approach. We can find peculiarities if we look at particular companies, but if the mining industry is to survive the profits from the few which succeed must in the end exceed the ones from those that fail, and while there have been no recent figures on the percentage of success so that one could in some measure estimate the element of hazard or risk involved in mining, there was as I mentioned this morning the Mutch Report of the Ontario Mining Association of 1943 covered all the metal mining corporations in Ontario from 1904 to 1941, which I think we would all agree was the growing period of mining in Ontario. In that period there were 4,426 metal mining corporations in Ontario, and only 41 of those companies were economically successful -- and economically successful was defined as those that paid any tax whatsoever. That is less than one of every one hundred, and those figures are of companies that were incorporated. Furthermore, of the 127 metal mining companies which reached the stage at which profits became taxable, only 32.3% recorded earnings which enabled them to return their invested capital to the shareholders. Naturally, of course, that would

indicate that about two thirds of these few companies must have paid some tax on capital, but the important point is that these figures only relate to mining properties which warranted incorporation, and we are talking about an industry. If we were to include all the mining plans on which mining exploration has been carried out and compare that total with the number of successful mines, the chances of success can only be described as infinitesimal. Given enough encouragement to warrant incorporation of a mining company, the odds are still only one in one hundred of the enterprise being successful -- and I do not think there would be very much difference in these figures if they were calculated today. I think they are fairly representative.

MR. STEWART: May I ask this: If we were calculating figures today and if we went back 60 years, that would be one thing; if we were taking figures from today and were taking into account the fact that exploration today presumably is carried on by methods and through techniques which have developed immeasurably during the last few years, would the situation be materially different?

MR. DIX: I can give you just a personal opinion there, Mr. Stewart. I am sure other members would be glad to add their comments. I have been in the business since I was a boy; it is only 35 years but it is quite a long time in Canadian mining. I would say that the hazards for the future in this business are equal if not more than the hazards in the

past. One of the important differences as far as Canada is concerned between the next 50 years and the past is that we have covered a great deal of ground in the past 50 years and we have eliminated a lot of areas where perhaps some of the luckier ones have already been found. It is much more difficult to find a mine today. The basic hazards, I think, are still with us and will always remain in our industry. We still have to have men of vision, men of courage, men who are willing to take the rigours of the bush. We have to have the and companies willing to risk their funds in order to replace the mines which are being depleted. It is a continuing process.

MR. STEWART: Let us concede that when we are dealing with a particular taxpayer in your industry, we must take into account in order to be realistic that there are a great number of people who have engaged in exploration unsuccessfully and have not reached the taxpaying category. Are we nevertheless not in the position, if the object of a depletion allowance in essence is to permit the recovery of cost over the period of production, that in Canada at the present time a good deal of the cost or amount invested will have been covered during the three year exempt period?

MR. DIX: The question whether depletion can be so simply defined I think is rather difficult, Mr. Stewart. The income tax department and

the mining companies concerned accepted the term depletion as a means to a certain end, and nothing was ever said to suggest that such a term had any reference or relationship to the amount of invested capital. I think it was recognized at the time that it was quite impossible, directly or indirectly, to estimate the life of a mine. That was a most difficult thing to do. If it were applied literally, it would probably be quite inadequate in most cases and perhaps excessive in all but a few, but in a solution of this kind I think we have to say in an average way we have to do practical justice to all concerned, and I think on an industry basis the question whether there is more advantage in depletion is one which is very difficult to answer because I do not think we are willing to recognize that it is just to get a return of capital. Capital is a continuing thing. We are dealing with wasting assets. Every ton of ore you take out means you are that much closer to the exhaustion of your mine and you are continually sinking your shafts and driving out into your new ore bodies. This is a continuing process in the mining business. As I say, the ones who do succeed must eventually pay for all who fail if people are going to remain in the mining industry or if we are going to continue to have a sound mining picture.

MR. STEWART: In other words, what you are saying is that depletion does or may permit the recovery for tax purposes of part of the amount invested, but it also serves as incentive to the industry?

MR. DIX: Right.

MR. STEWART: Then I think you will concede that whatever the purpose or purposes under our present Canadian tax structure, you do recover during the 3-year exempt period a good deal of the amount that was invested in the enterprise.

MR. DIX: This, of course, has no relation whatever to mines that have been in existence. This only is true in regard to new mines.

MR. STEWART: That is quite true, but it is true as regards new mines, is it not?

MR. ELLIOTT: If they are profitable.

MR. STEWART: Percentage depletion is in no sense limited to the actual amount invested?

MR. DIX: It bears no relationship whatsoever.

MR. STEWART: Looking at the incentive aspects, I take it that you would consider that the depletion allowance here or in your industry is appropriate because the industry is a high-risk industry?

MR. DIX: I would agree with you that that is partially the reason for depletion. There are many other elements, all of which can be woven into a pattern. Again, I do not think you should just look at one or two of the successful mines; I think you have to look at a whole industry. And unfortunately the statistics on what has been done in exploring and developing new mines in Canada is really very very thin, but I know Mr. Bradfield himself has made quite an expensive study on this to indicate what the chances are

for success in mining new mines. I am sure Mr. Bradfield would be glad to elucidate on this risk element and tell us just how often we do find a mine and what we do spend to find a mine. I think, Mr. Bradfield, you have some knowledge of that and can give some first hand information on it.

MR. BRADFIELD: I am afraid I do not carry these figures in my mind. However, I think it is sufficient to say that everyone is aiming for the big chance; that is what keeps us all in the business and that is what inspires people to keep on searching in spite of unsatisfactory results from year to year. Some people go through life, a lot of companies continue their search without fortune smiling upon them at all. It is the big chance that keeps them going.

MR. WANSBROUGH: May I make a comment, Mr. Chairman? We also have in our group today someone who has been very close to this question of depletion, especially from the point of view of taxation in the function of the Income Tax Act of Canada, of which it has been a constituent element ever since there has been an income tax in Canada, and I wonder if it would be appropriate to ask Mr. Tolmie to speak to some of the points raised by Mr. Stewart.

MR. TOLMIE: I do not think I can add much to what has already been said. There is one element, however, which no one has mentioned specifically but it is inherent in the depletion allowance; that is, the discovery allowance, what is found when a successful mine comes into being. It is

this discovery value -- in one case out of a hundred or one case in ten -- which is the great prize, the great carrot, which keeps these hundreds and hundreds of foolish people investing in mining and prospecting when the odds are so much against them. If you look only at the one per cent of successful mines and draw statistics from those, you are ignoring the industry, you are ignoring the thing that makes the industry. I do not think that the sum total of exploration expenses laid out by all the people, successful and unsuccessful, has been compensated for by the sum total of depletion that has been written off or deducted by the successful companies. Therefore, as an industry, it is not sufficient compensation. In other words, it is not a cost recovery even looked at as an industry as a whole but it does act as a carrot, as Mr. Bradfield says, which keeps people searching -- and I do think that the man who is licky enough to discover that one prize has a discovery value far in excess of the money he spent. It is not to be valued at the cost in his case. If it were, he would have been foolish to go into this game because the odds are a hundred to one against him and he would be better putting his money into utilities, blue chips or government bonds. What happens when he does discover the prize and starts to mine it is that the depletion is recognition of compensation for using up wasted assets. When the mine has been discovered and they start to mine it, the big factor in the profit is the using up of that value, that capital value which

he has discovered in the ground. The profits of mining and milling are small compared with the profits, if you like, of taking a ton of ore out, out of which he gets perhaps 10 ounces of gold or 50 pounds of copper. The chief constituent in his profit picture is certainly the value of the mineral in that ore body that he has discovered, and therefore it would be wrong to say that all that was profit irrespective of the wasting nature of the asset which he discovered.

MR. STEWART: I would like to canvass with you gentlemen some points which have been raised about depletion allowances in the United States. You are no doubt familiar with the fact that depletion allowances and the tax treatment of the extractive industries generally has been under review in the United States for some time, and it may be that the same considerations which have led to a review there are material as far as our Canadian picture is concerned. One of the points which I understand has been made by critics of the depletion allowance in the United States is that when depletion was first permitted for tax purposes it was permitted so that the small man would be benefited. In actual fact, in the United States it appears to be the case that the person who benefits from the depletion is the large corporation. In your case, as I indicated this morning, it would appear that roughly one hundred companies in Canada are responsible for 95% or a higher percentage of the production of the industry, which is running around $2,000 million

or $3,000 million per annum so we have an average production of $20 million or $30 million per company of the producing companies. Is this the size of ccomapnies for which depletion was intended? This seems to me to be a pertinent question having regard, as I say, to the attack that has been mounted on this in the United States.

MR. EDMONSTONE: In our case it is not the big corporation that benefits; it is our 25,000 shareholders.

MR. STEWART: At the moment we are talking about the corporate taxpayer. The shareholders will benefit ultimately from the prosperity of any company, but the depletion allowance is a corporate allowance, or the one about which we are talking at the moment is a corporate allowance anyway.

MR. WANSBROUGH: May I make one comment? You referred to the 95 or 100 companies who present such a high proportion of the mineral output in this country. As a matter of fact, I would say of those 95 or 100 companies there are not more than 5 or 6 that are very large substantial companies, and a lot of them are extremely small companies. I do not think it would quite work to say that you take the average and therefore all companies roughly are producing $20 million a year. That is not the way in which it works, and you can throw in all the gold mining companies. There are some very small operations and, in the case of gold mines, very few which are profitable. I just mention it as a caution against this type of averaging you do.

MR. STEWART: I do not want to labour this point too much; I am just putting to you things that I have come across in my own reading on the subject. Let me come to another: Would you consider the after-tax returns in your particular industry are higher than the average?

MR. BENNETT: In relation to what? In relation to equity or total investment?

MR. STEWART: No, in relation to after-tax returns in the other industries -- I would say on shareholders' equity.

MR. ELLIOTT: After-tax returns statistics have been prepared by the income tax department and have been published. We have averaged those figures from 1953 to 1961, with the exception of 1958. The 1958 figure was missing because we were unable to get a copy of that publication. It was not a particularly good year for mines. Taking the remaining years and the after-tax return on the basis of equity invested in metal mining other than gold mines, the figure was 9.9% as compared with 9.3% for total manufacturing companies reported in the same publication.

THE CHAIRMAN: This is before tax?

MR. ELLIOTT: This is after tax.

THE CHAIRMAN: The figure is 9.9 for companies other than what?

MR. STEWART: Other than gold.

MR. WANSBROUGH: For mining companies other than gold mining.

THE CHAIRMAN: 9.3 sounds very high for total manufacturing industry.

MR. TAYLOR: Those were companies paying tax in each case.

MR. STEWART: Let me put again the argument in the United States in this connection so we can have the benefit of your comments upon it. If the after-tax returns in the mining industry are broadly the same as they are in other industries, it would follow that the pre-tax returns in the mining industry must be unduly low since you are paying tax at one third less than other industry because of this depletion allowance. The question has been raised in the United States whether in these circumstances there is a misallocation of the resources of the country, whether it is right to encourage in this particular way an industry which does not produce a higher pre-tax return. I wonder if we could have your reaction to that?

MR. DIX: I think, Mr. Stewart, you would probably get a very strong reaction on that because the proof, again, is in the pudding. The Canadian mining industry is one of our largest industries in Canada and the fact that we have these depletion allowances (which may vary as between a competent company to a great extent and a less competent company) nevertheless, the basic fact is that we do have a very strong, thriving mining industry. This is the prize for Canada, and to ask whether or not this is perhaps, vis-a-vis the depletion allowance, money

going down the drain, is putting it rather in a peculiar fashion. To what do you allude? Do you suggest -- looking at some of these United States critics -- that perhaps we are wasting our natural resources, or are we wasting effort in exploring for resources when perchance the basic return is so modest?

MR. STEWART: I emphasize here that I am referring to American sources. I do not think anyone in Canada would in any way minimize the contribution of the mining industry to the economy, and I certainly have no thought of doing it. However, as I understand this point it is that if the mining industry is taxed at say 33% while the rest of industry is taxed at say 50%, the question is whether an industry should be given that tax preference if its pre-tax return is not a high pre-tax return.

MR. MITCHELL: In the case of British Columbia we do not have, as you know, a sophisticated economy. It is not even comparable, for example, with the economy of central Canada let alone with that of the United States. While this suggestion of the undesirability of continuing to support the mining industry or to give it a tax concession. While this suggestion of perhaps the undesirability of continuing to support the mining industry or to give it a tax concession might be applicable in some parts, the economy of British Columbia, because of its physical condition and distance from markets, is not yet developed and may not be developed for years to a position where it can be anything but entirely

dependent on the basic resource industry, and to suggest that the money the government does not get by reason of tax concessions could perhaps be better invested elsewhere would certainly beg the question: Where else in our area.

MR. STEWART: Let me read to you in this connection a paragraph which relates to the tax treatment of the extractive industries in the United States generally. What I would like to read to you now does not relate expressly or solely to depletion. I am reading from a booklet entitled The Federal Revenue System -- Facts and Problems. 1961, which is a publication of the United States Government Printing Office and contains materials assembled by the committee staff for the Joint Economics Committee of the Congress of the United States. This is the paragraph appearing at page 93:

> "One of the major criticisms directed against the present tax treatment of income from extractive industries is that it encourages serious misallocation of resources. It is contended that the present preferential tax provisions encourage a level of investment in these industries at which the pre-tax rates of return is substantially below that prevailing on the average elsewhere in the economy, although the after-tax rate of return, by virtue of tax preferences, is about the

same. Present tax provisions, in other words, encourage committing to development of mineral deposits real resources which would produce a greater, more valuable product judged by the preferences stated on the market in other lines of activities. Preferential tax provisions therefore are in fact a subsidy which promotes over-investment in the extractive industries."

That is the end of that paragraph. These are not my words but I wanted to put them to you because they are rather trenchant comments.

MR. EDMONSTONE: What are you going to do with the 60 or 70,000 thousand people who are dependent on the industry? Are we going to have them running restuarants in Ottawa?

MR. STEWART: I am not going to suggest to you that this industry is anything but a boon to Canada, but this Commission does put things of this sort to you in order to obtain your answers.

THE CHAIRMAN: We wish to know if the assets of this country are being misallocated. It is a very important matter and we would certainly welcome comments upon it.

MR. FOSTER: When you refer to our tax of $33^1/3\%$, you neglect to add to that the mining tax we pay to the province which makes our tax total greater.

MR. STEWART: Mr. Foster, I hope I am not forgetting anything. The provincial taxes have

not been mentioned until now but I think what we have to do on this Commission at any rate is to look at this situation as a whole, and I am anticipating a little what I will come to at a somewhat later stage. We have discovered so far today that for your industry -- and I am going back to the Federal sphere -- we have a three-year tax exemption which is not duplicated in the United States; we have a system of exploration and development allowances which, it was conceded this morning, was at least as liberal as that in the United States; and we have a depletion system which may or may not be better but apparently may not be any less liberal than that of the United States. I think this is perhaps a minor point, but it has appeared as we have gone along here that you have capital cost allowances in this industry which are higher than those for comparable assets in other industries. If statements of the sort that I have ventured to read to you can be made in the United States, if on balance our allowances or tax incentives to your industry are at least as great as those in the United States -- and at the moment they appear to be greater because of this 3-year period -- then surely if these questions are pertinent there we have to consider them here.

MR. EDMONSTONE: What about the substantial duties to the manufacturing industries? Are they not incentives too? I am referring to import duties.

MR. STEWART: Yes, please do not misunderstand me because I do not suggest that what has

been built into other industries in Canada may not be material when we look at the overall picture, but at the moment I am concerned with the broad question whether on balance equity is being done as between your industry and other industries and other taxpayers in Canada.

THE CHAIRMAN: Did you purposly overlook capital gains tax, Mr. Stewart, or the lack of one in Canada?

MR. STEWART: No, it might have been mentioned.

THE CHAIRMAN: It seems to me it might be the most important one of all after Mr. Tolmie's remarks concerning discovery value.

MR. CORISTINE: We must not forget our very substantial sales tax which does not hold good in the United States.

MR. STEWART: And which in your case has become more substantial.

MR. WANSBROUGH: There is one thing that has bothered me about this analogy between Canada and the United States. I think it is fair to ask us whether this applies to us in Canada and so on, but from what I have heard and read the depletion issue has been for so long a hot potato in the United States for reasons which do not apply in this country to the same extent at all. I have an idea that the fire under which the depletion has been for so long in the United States is something like a revolt of all the

other states against the state of Texas and most of this trouble in the United States has been centred not around the mining industry as such -- which I might say is very strongly protected not only by tariffs but by voters to some extent -- it centres around the oil industry. Therefore I just wonder a little about the complete pertinence of putting to us questions based on an American analogy which has a different history and where economic and national development is at a very different stage from the stage we are in at the present time. After all, there are many more phases in that complex matter in the United States to which "resourceation" can be applied with more effect than here. I think the origin and pertinence of those questions is one thing in the United States and quite a different thing in Canada.

MR. STEWART: I accept that. We have to deal with each country on its own merits. However, let me just read to you another paragraph which appears at page 100 of the same publication. This struck me when I read it as being pertinent, having regard to the position of the mining industry in Canada:

"It has also been suggested that a 3-year income tax exemption be substituted for present percentage depletion on new mineral deposits. Taxpayers would be permitted to exprnse exploratory and development costs, as under the present law, and would be exempt from tax on the first three years' income from the mineral property. Thereafter,

however, no capital recovery allowances of any sort would be permitted."

Here the committee obviously considered or was expressing a view which has been developed that under American circumstances it might be reasonable to give a 3-year tax holiday for new mines, but that once that had been given there should be no further depletion allowance. Granted that Canadian circumstances may be different from American circumstances and they may be materially different, here we are in the position that we have the 3-year tax holiday and we also have a depletion allowance. It struck me as being again a pertinent point.

MR. WANSBROUGH: It is the American Government reasoning, which we would not like to see followed in this country.

MR. STEWART: This is a sort of working paper of the staff of a Congressional Committee, not American Government reasoning. And I hasten to say that at the paragraph which deals with the taxation of the extractive industries does not go along all one way. They argue in favour of the continuance of the existing system just as they argue against. I have, I concede, been putting to you some of the passages which are critical of the present system because I wanted to get your reaction.

MR. EDMONSTONE: I think a pertinent remark here is that the iron mining industry in Minnesota and Michigan are doing everything in their power at the present time to bring the industry back

home. This should be some indication.

MR. STEWART: When you say "bring the industry back home" you mean to discontinue operations outside the United States?

MR. EDMONSTONE: That is right.

MR. ROW: Does it not make a difference that in some cases the United States are importers and in Canada we are exporters, and therefore assistance given to metal mining in the United States may be another form of subsidy -- import quotas and import duties?

MR. WANSBROUGH: They are getting so depleted in many mineral resources in the United States that if we do not flourish here they will have no one to fall back on half a century from now.

MR. STEWART: I should have thought if they were becoming depleted this should be an argument for additional incentives.

MR. ROW: It is cheaper to get them -- subject to national security -- from outside the country.

MR. STEWART: I am sure on that point, as on most, there are arguments both ways.

MR. CORISTINE: I do not think the mining industry in the United States plays the same role in opening up isolated areas as the industry in Canada, certainly with an economic cost to Canadian industry.

MR. BRADFIELD: Might I suggest, Mr. Chairman, that there is one thing of which sight is often lost in the United States -- and it applies to the United States in a lesser degree than to Canada -- that is that any tax that mitigates against the mining

of marginal ores. Even the best and largest higher grade mines, as a rule, have some marginal ore in their area. We in Canada have a number of mines which are distinctly on the edge. I think that this is something that frequently is forgotten. Taxes in any form have the effect of classifying some ores as non-commercial.

THE CHAIRMAN: Mr. Bradfield, do you not think you can extend that to all forms of activity apart from mining? It seems to me that taxes must depress almost all activity in which we engage, and certainly it is frequently represented to us by all kinds of industry that it is depressing of their particular industry and the less profitable units of the industry are bound to be the ones which are most affected. None of us really feels that taxation is anything except oppressive or depressive. We cannot do anything, no matter what we recommend, other than shift the weight of taxes from one person to another.

MR. BRADFIELD: It does seem to me where you have new wealth that is there for the taking, that you have the plant and facilities all set up but there is a slight margin here, it does seem wasteful if we are precluded from creating that new wealth by some tax that has that effect.

THE CHAIRMAN: The best that the country can do for it is not tax it. The second best is only to tax the profits resulting from it rather than the cost.

MR. STEWART: One of the suggestions made in this booklet to which I referred in regard to extractive industries is that the tax preference which now exists should be terminated and some sort of governmental subsidy or subsidies should be substituted. I was struck with the fact that on page 4 of your submission you were quite emphatic that you considered the best method or the best way of stimulating exploration and mining activity in this country is by tax incentive methods as opposed to subsidies or other indirect government assistance. Could you indicate why it is that in your particular circumstances you much prefer the tax incentive route.

MR. ROWE: We feel we know more about mining than do the government people.

MR. STEWART: How does that tie in? I am not sure that I am following that.

MR. ROW : Well, the tax incentive is out in the hands of mining people. Mining people are given the opportunity themselves to search out the opportunities for profitable extraction, whereas if the benefits were derived by way of government activity --

MR. STEWART: Or by government subsidy?

MR. ROW : Or by government subsidy --

MR. STEWART: Would they not still be free to carry on in what manner they chose but having the benefit of governmental financial assistance?

MR. ROWE: That would depend on the

nature of the subsidy.

MR. WANSBROUGH: There is partly a psychological reason for this. The experience we have had of government subsidy has not been happy. I refer in particular to the Emergency Gold Mining Assistance Act. One always thinks of a government subsidy as something brought in to help an industry in distress and sick -- and so it applies to the gold industry with which we are not personally concerned. There is of course the fact that a government can terminate rapidly; of course, all this can be terminated rapidly but the history of government subsidies does not lead one to have much confidence in their continuity. This kind of reason tends to make people suspicious of government subsidies, and there is the additional fact that there are usually some conditions attached to a government subsidy, conditions of control which are not always in the best interest of those who are controlled.

THE CHAIRMAN: The advantages secured under E.G.M. Act could not be secured under taxation though, is that not so?

MR. WANSBROUGH: That is quite true. Many of the companies now are in a non-profit position with E.G.M.A. and a lot of them would be dead if it were not for E.G.M.A.

MR. PARLEE: Is there not an analogy between mining incentive and research incentive rather than subsidized research? A tax incentive has been a greater incentive than a subsidy.

MR. STEWART: I think there is an analogy and I will put it this way. Where ever this Commission finds that preferences exist in an existing tax structure, I think it is bound to consider those preferences and to consider how they came about and whether on balance they should be continued, because, as the Chairman has indicated, if one taxpayer gets a preference this basically must be at the expense of other taxpayers.

One other point on depletion which I would like to raise with you is this. Our present percentage depletion, as we know, is not related to the amount invested in a particular mine. In the particular circumstances which again may be unusual, it may result in the benefit or benefits obligating several times or many times the investment in the particular mine. Again, in the American publication to which I referred it has been suggested that if the percentage dpeletion method is continued, there should then be some ceiling on the amount which can be recovered -- the ceiling being related in some way to capital cost. Perhaps it should be two or more times capital cost, but it should be assumed. Have you any particular comment on that?

MR. DIX: Would you perhaps offer some idea as to how you define capital cost?

MR. STEWART: I am perhaps expressing myself inaccurately. Let us say you have a particular investment in your particular mine, leaving aside for the moment the fact that part of that investment can

be recovered in Canada, without tax at all, a part of it may be recovered by virtue of section 83a. There is a residual amount. If we are proceeding on a percentage depletion system as opposed to a cost depletion system, should the amount that can be recovered under percentage depletion bear some relation to what could be recovered under cost depletion?

MR. ELLIOTT: I suggest to you the difficulties Mr. Dix has raised are insuperable and are the basic reason why the depletion or some form of it has been introduced into both Canadian and United States tax legislation, and I believe in other countries as well.

MR. STEWART: Is it not the case, Mr. Elliott, that in the United States you take them over on a cost percentage depletion?

MR. CORISTINE: No, you lose cost depletion, but it is not the lower of one or the other.

MR. STEWART: I thought earlier on you agreed with me that the American system involved cost depletion on a unit of production basis on the one hand or percentage depletion on the other, and that you took the lower of the two.

MR. CORISTINE: I certainly did not intend to make that statement, Mr. Stewart. You can have either cost depletion or percentage depletion, but you do not have to take the lower of the two. Inevitably cost depletion would be a lower figure than percentage depletion to the extent that you have profits.

MR. STEWART: I think perhaps I may

have gone too far in agreeing with you earlier. I come back to my American publication and I read now from Page 89 under the heading "Depletion Allowances." This was in 1961 and the position may have changed:

"Capital invested in natural resource properties may be recovered tax free through depletion allowances. For mineral properties these allowances are computed according to a cost depletion or a percentage depletion method, the taxpayer being required to take the higher of the two."

MR. CORISTINE: The higher?

MR. STEWART: The higher; I am afraid I gave way to you but perhaps I should not.

"To compute allowable depletion under the cost (or unit) basis for either minerals or timber, the adjusted basis of the property which would be used for determining the gain upon the sale of such property is divided by the total estimated remaining units (i.e., barrels of oil, tons of ore, board-feet of lumber) and the result is multiplied by the number of units sold during the year. Cost depletion deductions are exhausted when the adjusted basis of the property has been reduced to zero."

That is the end of that quotation and I do not want to make anything of it except to say that apparently in the United States it is possible, in fact it appears to be mandatory, to determine what your depletion would be on a cost depletion basis.

MR. CORISTINE: It is cost depletion

or percentage, which ever is higher. As a practical matter, percentage depletion is nearly always the higher, so you take that.

MR. STEWART: That may be so. I think you or someone was suggesting just a moment ago that cost depletion was not material in the United States and it does seem to me from this that it is.

MR. CORISTINE: I do not think it is as a practical matter because almost always percentage depletion is higher, and to the extent that you take percentage depletion it wipes out the basis on which you can take cost depletion. If your property costs a million dollars, the extent to which you get percentage depletion wipes out cost depletion.

MR. STEWART: I think we became involved in this when Mr. Dix asked me what amount can be depleted and I put this to you: What could be depleted would be the amount on which cost depletion would originally have been available, with perhaps suitable modification as we go along. It is certainly suggested here that there should be a ceiling on the total amount which can be taken by way of depletion if the percentage depletion method is continued. Another suggestion which is made collaterally is that the current rates in the United States, which as I indicated go up in the mining industry to 23% at the moment, should be reduced and perhaps the ceiling rates in that industry should be 15%.

MR. CORISTINE: Which is still more than we get in Canada -- the 15% gross. The fact that

the petroleum industry is going off gross depletion rather than the present net, I think is a good indication that they feel it gives more depletion.

MR. STEWART: We have only heard two representatives of that industry so far and they I think did not comment on that particular point; that is my recollection.

Mr. Chairman, that is all I will attempt to put at the moment on the question of depletion allowances for mining companies. I would now propose, subject to any questions the Commissioners have, to go on briefly to the question of shareholders.

THE CHAIRMAN: I have one small matter here and the others may have some other matters.

It is said that all deposits are not subject to percentage depletion. I think I now know what an ore deposit is but I am not very certain because coal comes within the sphere of an ore deposit.

MR. WANSBROUGH: Coal has a special depletion of its own, 10 cents a ton.

THE CHAIRMAN: That is a cost depletion.

MR. STEWART: It is an arbitrary allowance.

THE CHAIRMAN: Limited to the cost of the primary assets, is it not?

Is there anything else of substance which would be in the nature of an ore deposit? I am seeking to find out what minerals are not subject to 2% depletion.

MR. STEWART: My understanding is that coal mines have their special rate, which does not appear to relate to cost. Then if you have ore minerals and ore deposits -- and this is the type of thing you mentioned this morning -- they are not entitled to depletion as such but they do obtain Schedule E to the regulations with regard to capital cost allowance, on a basis which permits them to recover cost over the life of the deposit.

THE CHAIRMAN: That is right. That is not percentage depletion; it is restricted to cost depletion. Therefore I am anxious to find out whether there are any important minerals which, because of the nature of their deposits, do not obtain to a percentage depletion.

MR. WANSBROUGH: I think there are very few left if I may say so, especially in relation to the clause, because over a number of years they have always said all deposits except -- and then they have been lengthening that group of exceptions, and I think within the last year gypsum was added. I think it would be possible to find out what exceptions remain.

THE CHAIRMAN: Thank you very much.

COMMISSIONER GRANT: I would like to ask what mining is now being done on the open cut basis. Is practically all the new development of iron ore in Labrador open cut?

MR. DIX: Yes.

COMMISSIONER GRANT: To date, you

have not been able to deduct the open cut development expense? Since that open cut method of development was used, have you been able to deduct the cost from current income?

MR. ELLIOTT: The company in open cut mining must deduct all its expenses and defer none within the pit limits, whereas underground you may defer such things as shaft and main haulageways and other underground works of a similar nature. It is a question of deferring to a time when the company is taxable rather than not being able to deduct it.

COMMISSIONER GRANT: On page 10 you mention that the mining industry spends $45 million on exploration in an average year. Do you include in the exploration cost of $45 million, work that is done by way of extending your ore body within the mine itself?

MR. DIX: No, this is exploration and that is outside exploration.

MR. STEWART: In connection with shareholders' depletion, you make two points. One is that in the computation of income for the purposes of that allowance, Section 83(a) expense should not be deducted. I realize that we touched on this a little earlier and if the reason was given I am afraid I have forgotten. Why do you distinguish between the shareholders' allowance and the corporate allowance in this respect?

MR. DIX: Insofar as Section 83(a)

is concerned?

MR. STEWART: Yes.

MR. DIX: I think we make two suggestions with regard to shareholders' depletion, and I think there is a similarity in both of them. In Section 83(a) a company may not in one particular year have taxable income or may even have a tax loss and shareholders' depletion is calculated on the basis of the percentage of mineral profits, or shall we say a mineral content of its income in a year prior to which dividends were declared. Consequently, let us assume that in 1963, for example, the shareholders' depletion rates are calculated by reference to its previous taxation year, if in that previous taxation year by a series of circumstances, one of which might be Section 83(a) that company had a tax loss. Then in effect there would be no taxable income in that year, and my reason of that the shareholder, even in 1963 when profits were such that dividends were paid, would get no depletion allowance whatsoever. It is just because of the vagaries of the definition of mineral profits and how it is defined that we are suggesting these two minor corrections to remove an inequity which has existed on occasion in shareholders' depletion.

MR. STEWART: Mr. Dix, Section 1500 of the regulations --

MR. DIX: Part 13 on page 77.

MR. STEWART: Yes, "grants a deduction where mineral profits are within certain

percentages of income". Would it follow from what you have just said that you would wish to exclude Section 83(a) both for the purposes of determining mineral profits and for determining income?

MR. DIX: For both purposes?

MR. STEWART: Yes.

MR. DIX: Mineral profits, of course, are defined in 1303, and the anomaly in regard to Section 83(a) is only in respect of those companies who, though they may have had a substantial surplus in previous years, may have had a bad year, and it would be more pronounced if section 83(a) had to come off before mineral profits were determined. So the only suggestion we have is that it would remove an inequity if at least Section 83(a) were not deducted before one determined mineral profits as defined in 1303 of the Regulations.

MR. FOSTER: May I add that it says that Section 83(a) must be deducted in respect of income in full. This is where an anomaly is created. There is no taxable income and therefore no mining income. You could defer some of the capital cost allowance, but if you do not take it all on 83(a) you lose it completely, so to provide depletion for shareholders you have to sacrifice some of 83(a) or be trapped by the section.

MR. STEWART: I am not sure I have altogether followed this, but I think perhaps I can work it out from the record. If not, perhaps we can come back later.

MR. DIX: By all means.

MR. STEWART: As I understand it, there is nothing of a comparable nature under the American tax system to this shareholders' depletion.

MR. CORISTINE: No, there is nothing comparable.

MR. STEWART: I would like to move on to the question of the exemption to prospectors and grubstakers for a monent. Could you indicate to us how significant this particular exemption is today? I realize in the past it has been of considerable importance, but is it of decreasing importance in your industry?

MR. ELLIOTT: I would say it is still of considerable significance. Still a great deal of exploration is done by others than producing mines and the protection this gives to the grubstaker and to the prospector is of paramount importance. I think if that were removed, then the prospectors and the independent -- if you like to so call them -- prospecting organizations would disappear from the field. After all, they have been very important in finding, even though a large company may eventually develop the mine. They have been important in finding mines. I think it is correct to say that very few of the mines producing today have not been pointed to at least by the individual prospector, whether he was working on a company payroll or not. Usually those working on a company payroll receive a minimum salary. They take a lower salary in order to get an interest in

anything they find. That is the incentive that takes these fellows out into the field and keeps them there through black flies and mosquitos looking for the jackpot.

THE CHAIRMAN: You suggest if he was taxable on that he would not do it?

MR. ELLIOTT: If he was taxable on that he could not afford to do it. If he had to pay all the tax in one year, he might just as well not do it.

THE CHAIRMAN: It might be averaged.

MR. ELLIOTT: Even if one found a basis of averaging, I think that the psychological basis would be the same.

THE CHAIRMAN: You say he would not do it if he was taxed?

MR. ELLIOTT: No. He pays tax on his salary, but to tax him on his finders' profit --

THE CHAIRMAN: It has been represented to us that a good inducement might be to allow monies that have been put up and lost to be fully deductable from other income. That might provide more monies for this type of exploration. I would have thought that would be a pretty fair inducement and I would have thought that if that were done it might be a stronger inducement than freedom from tax. I am inclined to think that people prefer to find someone to share the cost with them than to not give up part of the reward. It seems to me easier to part with some of ones reward if one can have

someone to share ones cost -- and from what you have said, there would seem to be a very much greater debit in this sort of thing than there is benefit.

MR. ELLIOTT: One has to think of two people. There is the prospector or the mining engineer who earns interest in any claims or stakes he acquires, and then there are those who back private individuals or experts in companies. In any event, the number of prizes are very very small. A few prospectors, particularly those on their own, will stake favourable claims and be able to make a good deal, which keeps them in the business providing it is not taxed. The minute you tax that, those people will disappear from the scene.

THE CHAIRMAN: I do not think you would ask that the monies would be deductable and that the monies be not taxed. Surely that would be getting it both ways and that would be unfair to the rest of the community. I gather from what you say it is more of an inducement to have the results tax free than to have deduction or costs.

MR. ELLIOTT: I am talking about the prospector and the grubstaker, not a producing company.

THE CHAIRMAN: I think I am too. I am thinking of the individual. A grubstaker is a man who will go out and see, and I think that individual is not now permitted to deduct the money which he hands out.

MR. ELLIOTT: That is right.

THE CHAIRMAN: It has been suggested to us that it would be great encouragement if he were permitted. But I would think it would be unfair to permit that and also permit exemption of awards from tax. I am seeking to find out what your opinion is, which of the two would be more useful.

MR. ELLIOTT: My opinion is, as far as those two types of concern are concerned, that the present exemption provided here is more of an inducement than the cost deduction.

COMMISSIONER GRANT: We were also approached with a view to having cost of prospecting and grubstaking deducted, regardless of whether there was any find. I take it if there is a find and if it proves to be acceptable, it is part of the expense of bringing the mine into production and it would be deductable in that case.

MR. ELLIOTT: The original prospecting about which I am talking does not become deductable.

COMMISSIONER GRANT: It is still not an expense?

THE CHAIRMAN: No, because the income is not taxable.

MR. ELLIOTT: It is only deductable to the extent --

COMMISSIONER GRANT: The point I was really coming to was this: My recollection is that prospecting today is quite different from prospecting in the old days when the prospector went

out with his hammer and his pack. Today a great deal is being done with the use of aeroplanes, and therefore it can run into a great deal of money -- and that is for the private prospector.

MR. ELLIOTT: That is true, but he covers a great deal more ground and he has to raise more money for a grubstake; that is quite true.

COMMISSIONER GRANT: Sometimes the aeroplane is used for purposes other than prospecting.

MR. ELLIOTT: Very few outside of the larger companies own their own aircraft. There are about a thousand aircraft across the country and one just gets into them like one would into a taxi. The individual prospector still has to work along the ground pulling off the moss and looking at rock exposure.

MR. STEWART: Mr. Chairman, I have covered the points I wanted to raise on matters which relate peculiarly to this industry. As you know, there are other points made in this submission or these submissions which are of a more general nature but it would not seem to me that we need go into them at this stage. I think I understand them and that the Commission staff understands them.

COMMISSIONER WALLS: May I ask one question to clarify? In regard to your representations with regard to sales tax, I am interested in "Materials (including complete parts of machinery...) consumed or expended directly in the process of production" to be exempt from tax, because of course in most

industries the materials consumed are exempt. Were you thinking of such things as grinding wheels when you made that reference?

MR. BENNETT: One of the problems here is that the use of the word "consumed". You may recall before these exemptions were removed that exemptions were building materials, production machinery and apparatus and materials consumed in production. Between the first announcement of the budget and the announcement of the modified budget the exemption was restored on consumables, materials consumed in pro-udction, and a graduated tax was made applicable in place of the immediate application of 11% tax. When you come to look at the things that you use in the course of production and you compare these things to these two rather arbitrary listings, immediately you find there is a number of things consumable, and by that I mean they are used up quickly in the process of manufacturing, things that are in the production and machinery list and are not exempt, and they are just as much consumable as some of the items on the other list where the exemption was restored.

COMMISSIONER WALLS: That is the point I was trying to get at because there is quite a similarity, I must agree, between a grinding wheel such as I have seen used in your mines and, and grinding balls, and the fact is that they allow exempted grinding balls or rods for use in ball and rod mills. In other words, they tax a grinding ball, and other abrasives are exempt. The difficulty we

are up against here, it seems to me, is that when it stops being a material used and when it becomes a machine part, and now machines are taxable it would be rather hard to exempt parts of machines, as it is a matter of definition, unless one is going to exempt the whole machine.

MR. BENNETT: There is a simple rule and we proposed it at the time the bidget was being reconsidered -- and I think that is the proper description of that process. This is the simple rule of anything the Income Tax Department allows you as expense would be exempt, whereas anything that you would be required to treat as capital, anything that you capitalize, would not. We would prefer to go back to the situation prior to the budget. We rather thought this was too much at the time. This looked to be a reasonable solution and it seemed to satisfy this difficulty that you are raising.

COMMISSIONER WALLS: It is a matter under consideration by our research staff and by the Commission as a whole. Your ore products are exempt, and your gold and silver ingots, and the only point I would point out -- as we have pointed out to some other groups who made the same recommendations -- is that there is a number of other leading export countries who do tax machinery of production without adverse effect on exports.

MR. BENNETT: You have to consider your whole range of taxes. I think this business of looking at what is done in the United States in

terms of 3-year exemptions is a small part of the story. Industry, to be in a competitive position, has to be judged in relation to the whole range of taxes -- provincial, federal, sales and so on -- and only then can you arrive at a fair comparison of the treatment an industry gets here in comparison with other countries.

COMMISSIONER GRANT: I have one more question. This question that I have to ask has to do with a 100% foreign/loan owned subsidiary. I do not know whether there are any such companies operating, so therefore my question is not aimed at any one company, it could be almost hypothetical. Is there any danger of the situation where the product is being exported out of Canada and is owned by a company -- the operating company in Canada is 100% owned by a foreign corporation -- of pricing out taking place in respect to that product so as to keep down a reasonable profit?

MR. CORISTINE: I think members of the National Revenue were very aware of that problem, and they follow it closely.

THE CHAIRMAN: Section 17?

MR. CORISTINE: Yes. There are provisions in the Act to prevent transfer of profits abroad artificially.

COMMISSIONER GRANT: I did not know whether it affected the mining industry. I know it is a factor in the paper industry.

MR. CORISTINE: Yes.

THE CHAIRMAN: There are no more

questions from the Commission. It has been a very interesting day for us and I think it is noticeable that you made no reference to capital gains at all. We have had a good deal said to us about the desirability or otherwise of taxing capital gains. I think we must assume you are neutral at the present time.

MR. EDMONSTONE: We are not neutral; we are very much against it.

THE CHAIRMAN: Are you all together on that?

--- Several MEMBERS . Yes, very much so.

THE CHAIRMAN: You would be surprised at the responsible bodies not with you. If you watch the submissions put to us you will see. I am not prepared to accept a statement from you lightly, but if you are all together I will be prepared to take it as your considered view. It is not an open or shut book and not something only recommended by labour unions and that kind of thing; there are all kinds of people talking about it.

Thank you very much. It has been a very interesting day. We have given it consideration and we continue to do so. If we have been aggressive in our questions, it is not because we have preconceived views. We have a job to do, and we consider this fully.

MR. WANSBROUGH: We appreciate very much the interest you have shown. We also have had

an interesting day. Thank you for having us.

THE SECRETARY: The British Columbia Yukon Mines were not able to appear before you in Vancouver. They sent their brief which I now enter in the record as Exhibit 275.

--- Thereupon the hearing was adjourned at 4.20 p.m.

# ROYAL COMMISSION

# ON

# TAXATION

## HEARINGS

HELD AT
OTTAWA

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VOLUME No.:
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# THE ROYAL COMMISSION ON TAXATION

Hearing held in the Centre Court Room, Exchequer Court of Canada, Supreme Court Building, Wellington Street, Ottawa, on Tuesday, the 3rd day of December, 1963.

## C O M M I S S I O N

MR. KENNETH LeM. CARTER -- Chairman

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S. M. MILNE

MR. CHARLES WALLS

## LEGAL COUNSEL

MR. J. L. STEWART

## RESEARCH DIRECTOR:

PROF. D. G. HARTLE

## SECRETARY

MR. G. L. BENNETT

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## INDEX TO EXHIBITS

---Upon Commencing at 9:30 a.m.

THE CHAIRMAN: All right, Mr. Secretary, we will start.

THE SECRETARY: Mr. Chairman and Commissioners, the brief before you to-day is being presented by the Board of Trade of Metropolitan Toronto. Mr. John Taylor, First Vice-President of the Board of Trade, is here to speak to the brief.

Associated with him are a number of colleagues which he will introduce to you. I would like to enter this brief into the record, Mr. Chairman, as Exhibit 276.

---EXHIBIT NO. 276: Brief of the Board of Trade of Metropolitan Toronto.

SUBMISSION OF

THE BOARD OF TRADE OF METROPOLITAN TORONTO

Appearances:
MR. J. KERR GIBSON, Chairman, Taxation Committee.
MR. JOHN W. GRAHAM, Q.C., Vice-Chairman of the Taxation Committee.
MR. A. C. CRYSLER, Q.C., Legal Secretary of the Board.
MR. JOHN KIRK, Vice-president, CCH Canadian Limited.
MR. JOHN TAYLOR, 1st Vice-president, Board of Trade.

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, Mr. Taylor and gentlemen. We are glad to see you here. We have read your most interesting submission and we would like to discuss it with you. Before doing so, I will introduce to you our commissioners, whose names are all before them. If you would like to speak to your submission we would be very glad to hear it.

I see you have prepared some remarks, and we have not had a chance to read this. I would be very glad if you would present them to us.

MR. TAYLOR: Mr. Chairman and Members of the Royal Commission on Taxation, I sincerely regret that our President, Mr. Geoffrey Phipps is not here in my stead. This was intended, but unfortunately circumstances have made it impossible so I am substituting for him as the leader of our delegation.

On behalf of the Board I would like to thank the Royal Commission for according us this opportunity of presenting to you and discussing with you the Board's views on some of the aspects of the subject matter which you have under consideration.

Our delegation is made up of Mr. J. Kerr Gibson, C.A., the Chairman of our Taxation Committee - Mr. John W. Graham, Q.C. the Vice-Chairman of that Committee - and Mr. A. C. Crysler, Q.C., the legal secretary of the Board. Also present is Mr. John Kirk, Editor of Tax Reports CCH, a member of the Board and a valuable and hard-working member of our Taxation Committee.

With your permission, discussion of our brief will be carried on not by myself but by Mr. Kerr Gibson and Mr. John Graham -- but before calling on them I would like to make just a few comments.

First of all I would like to tell you that the Board of Trade of Metropolitan Toronto comprises a membership of over 10,000 persons. The principle classifications represented, and together they would comprise approximately 75% of the total membership, are financial,

manufacturing, professional and service trades other than retail. And since the interests of a great number of our members are not only local but also provincial, national and even international in scope, we believe we can fairly claim that the views of the Board of Trade of Metropolitan Toronto represent not only those of Toronto business interests but also represent the views of a major cross section of the business and professional interest of our Province.

The brief we are presenting to you originated within the Board's taxation committee. This committee is made up of approximately 50 people who have special knowledge of taxation and its relation to business. It includes executives, accountants and lawyers and their selection, to the best of our ability, is upon a basis ensuring that the point of view of each of the principle business interests in the Board is represented on the committee.

Following completion of the committee's deliberations, and these extended over many months, their draft brief was circulated to the members of the Council of the Board. Council is made up of 24 senior executives who again, to the best of our ability, are representative of the major classifications of business in the membership of the Board. After their study, the Brief, in the form in which it appears before you, was formally approved and authorized for submission to this Royal Commission.

Since the Board of Trade of Metropolitan Toronto is an organization representing business interests

in their practical day-to-day operations, and since its functions are not research in character, the comments in our brief reflect the views held by businessmen as a result of their practical experience. We believe that such views have a validity of their own and we have not attempted to thoroughly support them with statistics. In any event, in numerous cases and perhaps particularly in regard to the comment on capital gains tax, adequate statistics are not in existence. However, while we feel that statistical analysis does not by any means always represent complete treatment of a problem, we do agree that wherever possible the validity of suggestions should be tested by statistical analysis. We are satisfied, though, that such analysis will be in very competent hands with the excellent research staff assisting this Royal Commission.

I have no additional comments to make on any point not already referred to in the brief. However, for the sake of emphasis, there are one or two things I would like to add.

First of all, while the Board is conscious of the growing financial needs of the Provinces and the probable necessity for adjustment in financial responsibility and taxation in order to enable the Provinces and their municipalities to discharge their responsibilities properly, we are concerned and certainly hope that Federal/Provincial fiscal problems will be solved with due regard to proper co-ordination of taxation with the economy of the country and the avoidance of multiple administrative burdens and overlapping taxation

on the business community.

According to D.B.S. figures, the gross national product in 1962 was in the range of $40,400,000 and in the same year the total of direct and indirect taxes levied by the Federal, Provincial and Municipal Governments of Canada was in the range of $10,016,000. It would appear then that in that year these taxes absorbed approximately one-quarter of the gross national product --- and on top of this it should not be overlooked that taxpayers are increasingly required to make compulsory contributions not specifically categorized as taxes, to numerous and various health and welfare programmes.

It should, we think, be obvious that with such a proportion of our gross national product being taken in these ways, serious consequences can in certain circumstances result unless the incidence of the taxation is properly co-ordinated with the economy of the country. Also, to the extent that it may be found necessary for the Provinces to Levy taxes heretofore levied by the Federal Government, and particularly in the fields of direct taxation such as personal income tax, the tax on corporate profits and succession duty or estate taxes, it is of the greatest importance to avoid, wherever possible, increasing unnecessarily the administrative burden on tax payers and the overlapping of taxation on business

In conclusion, and as just an ordinary run-of-the-mill businessman, I would also like to take this opportunity of saying how increasingly concerned I

am becoming -- and as my business responsibilities increase and my business horizons widen I become just that much more concerned -- about the increasingly greater amount of time that high level talent in this country is required to spend on tax problems. Perhaps I should say on 'minimization of tax' problems. In any event, it seems to me a terrible thing that all this time and all this ability of so many people should have to be used in this way instead of in productive effort. I would certainly hope that in your findings you will include recommendations that will act to alleviate this situation -- a situation which of course is brought about by the too high taxation levels in certain areas and the too many and too complicated tax regulations that exist in this country.

This, ladies and gentlemen, is all I have to say, and now if I may, I would like to suggest that you direct any questions you may have in connection with the brief to Mr. Kerr Gibson, C.A., Chairman of our Taxation Committee.

THE CHAIRMAN: Thank you very much, Mr. Taylor. From now on I suggest you remain seated unless you wish to stand. You may stand if you wish to do so. Before addressing questions to Mr. Gibson, I would like to ask you one or two questions, I think, Mr. Taylor, appropos your remarks.

I have always thought, like you, that there is a tremendous amount of waste in the efforts of experts fussing around with taxation problems, but I have not really seen a statement made quite as closely related

to the percentage of G.N.P. which go into taxes. I must say you have almost convinced me that perhaps what looks to be wasted efforts is really fairly well spent when it is considered it is concerned with 25 per cent of the gross national product. It is true that we must do everything we are able to do to reduce it and make it as simple and as easy to understand as possible, but one can never make taxation so simple that it is not going to require a good deal of effort to keep ourselves on the track, I don't think.

You were very modest in your statements with regard to the capacity of run-of-the-mill businessmen, and I was not quite clear as to what you meant by the fact the Board of Trade functions are not research in character. I wonder when one's function becomes research in character. I suppose all organizations who speak to us must do a certain amount of research work in order to prepare whatever they put before us. Some, of course, doing more than others. Just what do you mean when you say it is not research in character?

MR. TAYLOR: I think what we meant there, in our Board group we do not have a department of economics or economists and statisticians who might in other circumstances have supported this brief with a vast amount of figures and graphs and charts and that sort of thing. This is what we meant to imply there.

THE CHAIRMAN: You have done pretty well I think. I would suggest that we approach this by taking it subject by subject, if the Commissioners

agree with me, and the first subject you put before us is entitled Capital Gains Tax.

You come down fairly strongly against capital gains tax for various reasons which you have set out in the submission. Does this mean you are satisfied with the law on capital gains as it now stands?

MR. TAYLOR: I think the answer to that is no, in part, we are not satisfied. I think that the Board discussed at some lengths -- our tax committee discussed at some lengths -- the question of whether we should make any suggestion at all as to how the very numerous appeals that arise out of the fine distinctions between taxpayers' intentions, particularly in connection with real estate transactions, and also in similar sorts of assets, whether we should try and make some suggestion as to how the volume of appeals on points of that sort could be cut down, and the degree of certainty could be introduced into that area.

We were not able to make a specific section suggestion in that connection, and first of all I think we concluded that to solve this problem, introducing legislation that would be specific in resolving taxation on capital gains would introduce other problems of a different nature.

We concluded we would be prepared or would prefer to stick with the system we now have, which does have some objections to it, rather than suggest the introduction of capital gains tax of any form which we feel would lead us in the wrong direction and towards the sort of objections we have to general capital

gains tax system.

THE CHAIRMAN: Some people have pointed out to us that there is a fair amount of income escaping tax, the income being that earned by speculators particularly in securities. It is pretty hard to ascertain the proof of that statement. Would you have an opinion as to whether there is much income escaping tax, and whether it would be possible, by further use of the existing laws, to bring that income to tax, or whether it needs a change of laws?

MR. GIBSON: I don't have an opinion of the amount or extent of the income that is escaping tax in this way. I do think that it depends on what one's idea of the meaning of the word "income" is.

There is no doubt a great many profits are made by people who speculate, particularly in marketable securities. Also I suppose a great many losses. Perhaps the profits exceed the losses, but I would be inclined, and I think the Members of the Board generally would prefer to regard profits made in speculation as non-taxable, as non-income, partly because of the incentive that this may produce to investors to engage in more speculative types of investments.

THE CHAIRMAN: I wonder if we are thinking of the same types of profit. I think there are various kinds. There are those, of course, made by professional people in business such as brokers and investment dealers, and I suspect generally those are taxed. I do not know that they are all taxed. Then there are the speculators who delve in no other apparent living,

who one finds chiefly in the offices of stockbrokers. I am told they make a good living and pay no tax. Are these the ones you are thinking of?

MR. GIBSON: No, they are not, and personally I would have thought where they could be assessed for tax on the results of their efforts, if it is profitable, they would be held to be liable for tax. I gather this has not been -- at least, the administration has not been particulary diligent in searching out this type of investor or speculator. However, that may be more for administrative reasons than for any rule of law.

Certainly I would not have thought that they were the real contributors to the investment pool of this country.

I do not think the Board feel very strongly about that area. I really suspect that their activities are such that they would be clearly covered by our present rules of law on the question of whether this is income or capital.

COMMISSIONER PERRY: Were we not told by the Inland Revenue Authorities in London they had taken people in this position to Court under the venture in the nature of trade wording, and failed to establish their case, that the Courts would not support them, that these people were carrying on a taxable business.

MR. GIBSON: I was not aware of that although I think the Courts have probably bent a little over backwards to avoid getting into that area. I am inclined to suspect, although I have no real ground for believing this, for having this conviction, that the amount of

profits that are generated by taxpayers in this way in normal speculative or business undertakings of this sort, or, let us say, an occupation of this kind, is pretty minor. That is a suspicion only. I have certainly nothing to go on.

THE CHAIRMAN: Well, I would think that you are probably correct there, but I wonder whether that should be the end of it.

It would seem to me that if the taxpayer or the public were aware of other people escaping tax, it has a bad effect on other taxpayers.

MR. GIBSON: I am sure the Board would not want to have it felt they were imposing all possible forms of tax that might be described as capital gains tax. If an extension to our present tax system to cover this type of profit were made, I don't think that the Board would have any particular opposition to it. I don't know whether the other members here --

MR. GRAHAM: Mr. Chairman, I would like to say in our discussions in our Committee, which extended over a number of months, there was no word uttered in defence of those who cause an appreciation in their assets by trading constantly and frequently and to their advance in securities, the type of person of whom you speak.

THE CHAIRMAN: Yes.

MR. GRAHAM: And my own personal view is that would be caught under the present legislation if the administrative problem was not too great, and it may well be that it is for the amount of revenue that

would result to the Exchequer.

We were much more concerned with the person who in a perfectly legitimate manner, for example, purchased real estate and sold it a few years later, and the line of demarcation is so difficult to draw, the feeling is the Courts have been tending in the direction of taxing these enhancements in value and getting awfully close to capital gains tax.

We, however, base our case far more generally. We do not feel that a capital gains tax, in the state the Canadian economy is in, is in the national interest. As we indicate at Page 7 of our brief, it may well be there should be some greater certainty and clarification in the legislation as a guide to those who are endeavouring to determine on a particular case whether it is income or capital, and this is very difficult. We do not minimize the difficulties of enunciating clear-cut rules.

THE CHAIRMAN: That is the next point I was coming to, as to what those rules should be. Most European countries have got rules which are essentially a time situation, a graduated time scale. The earlier you pay, the more tax you pay, running over a period of years, but very few rely on the sort of tests that we do in this country.

Whether theirs is better or not is very hard to tell. They are entirely different. In the U.K., which has moved from what could be said to be our system, or pretty close to it, to the other kind I was thinking of, they felt they could not make, as Mr. Perry has just said, their old system work satisfactorily. When one

tries to weigh up the advantages of leaving it the way it is, the way it is written into the Act, which I suppose is as good as can be conceived, to a more clear-cut solution, although highly arbitrary, there are a lot of pros and cons fall on either side.

MR. GRAHAM: If I may say, Mr. Chairman, from my own professional experience, there seems to be abroad a sort of man-on-the-street feeling that time is a very real factor. Certainly in the case of the builder. I am speaking now of the large builder, a man who builds apartment houses and buildings of that kind. Whether there is any sanction for this view, certainly many of them feel when they hold a piece of property for five years that they probably have escaped any suggestion that any enhancement would be regarded as income. Speaking, not on behalf of the Board, because we did not discuss this aspect of it, it may be that some basis should be established whereby there was a graduated percentage that could be regarded as income and a percentage as capital in the absence of affirmative proof to the contrary by the taxpayer.

I still think there should be an opportunity for the taxpayer to demonstrate this was fortuitous and solely in the nature of a windfall and was not really a profit resulting from an undertaking in the nature of trade. Something on that line would at least import some certainty into a very conflicting field.

MR. GIBSON: We did discuss at one stage whether some time rule should be introduced or maybe suggested as being a means of dealing with real estate

transactions, and particularly transactions in other commodities that are traded that are not normally bought and sold - at least not bought or invested in for income-producing purposes.

There is obviously one problem, if a time limit is imported without any graduated scale, it defers the time when there will be a sharp dividing line between those which will be taxable and those which will not, and I think fairly obviously it will delay the normal trade period. I think it is really an artifical impediment in a normal commercial transaction.

If a sliding scale of some sort is imported, presumably a smaller proportion of gain or loss would be taken into account. This would probably overcome a good deal of that.

Our concern and reason I think for not suggesting something along these lines was that we suspect, and perhaps through reports on the results or anticipated results of capital gains introduced in England, this would not be a revenue producer. The only real purpose to be served would be to remove feelings of concern on the part of some taxpayers that others were escaping tax on profits that should be taxed.

THE CHAIRMAN: Also it would introduce more certainty.

MR. GIBSON: Perhaps it would introduce more certainty into legislation, and this may be an extremely expensive way of doing it.

The elaborate administrative procedures that would have to be adopted to enforce such a provision we

think might very well overcome the advantages; outweigh the advantages.

THE CHAIRMAN: It could be.

COMMISSIONER PERRY: Have the witnesses gone far enough in their thinking to tell us what sort of capital gains tax they do not want to have? I think you are verging very close to some sort of capital gains tax. You also seem to be fairly opposed to some sort of capital gains tax. I wondered what it was to which you were opposed?

MR. GIBSON: First of all, I think we are freely opposed, and without question perhaps, to a general system of capital gains tax such as that used in the United States.

Obviously a good deal of our discussion and thinking was --

COMMISSIONER PERRY: That is not even a general system within a time period, with things being income on one side and capital gain on the other.

MR. GIBSON: There is a time period there, but all Canadians are taxable when it is realized I think with the exception of individuals who have capital or appreciated property at the time --

COMMISSIONER PERRY: But then there is a special rate, in my mind, of capital gains system which is something which says all receipts of income from no matter what source are taxable, period.

MR. GIBSON: And capital gains are regarded as income.

COMMISSIONER PERRY: Yes. Under that concept.

You started to make special provisions for treatment of certain forms of income, and then I think all you are doing is alleviating the impact of the tax on income arising from circumstances of the transaction. I do not want to be unnecessarily sure about this, but you are doing what the American system does.

MR. GIBSON: Basically, yes, and I am afraid we didn't direct our attention to the possibility of capital gains being regarded exactly as other forms of income because I do not think we really catalogued our reasons for feeling that would be unfair and unwise.

I think basically we think there is a valid distinction between capital gains and income, and tax on capital gains being in many circumstances, in any event, a tax or capital levy part of the income-producing property as being subjected to tax and extracted, and if this is so, if gains or enhancements in value of the income-producing property is subject to tax at the same rates and on the same basis as income itself, in what we regard as income from the use of property or productive effort. We would not think this equitable or desirable.

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Certainly graduated surplus of rates applying to individuals would seem most inappropriate.

COMMISSIONER PERRY: When you speak of a time period this is not really something put forward in your brief. You have in mind interposing some sort of time period within the present concept of what creates income or dealings on capital assets.

MR. GIBSON: As I say we discourage the thought that we might make some suggestion on the grounds we didn't really think this would be a significant improvement. While it would have some advantage in improving the degree of certainty as to whether taxpayers were taxable or not on transactions in real estate or securities occurring fairly frequently we felt the administrative headaches that it would bring about were probably not justified.

Our only purpose really in thinking at all along those lines was not that we felt a time period as such was a good measure as to whether a gain was taxable or not but such a rule might impart some certainty into an area that is becoming increasingly doubtful because of the trend in the Court decisions.

THE CHAIRMAN: Would that not by itself reduce the administrative effort, an awful lot of which is devoted to making certain things which are uncertain.

MR. GIBSON: I am inclined to doubt that. If the general system of taxation on gains, presumably in certain types of commodities only, perhaps it would be more general. If something were commenced I should

think it would extend to practically all forms of property, with perhaps exceptions in the form of residences and things of that sort.

Once it was introduced it would likely be extended to practically every type of property. But there would be required to have reporting of all transactions which might be subject to tax by taxpayers and checking of them. It would seem to me once you have started the administration would have to seek out people who have failed to report and this would add to the burden of the taxpayer.

THE CHAIRMAN: What kind of commodities are you thinking of besides real estate and securities, works of art?

MR. GIBSON: As I say we haven't really gone into this thing very thoroughly. We discarded it at a fairly early stage. We thought of real estate because it was the form of property that gives rise to the most of the problems that appear in the Court. Other types of property commonly purchased for appreciation are for personal use. I suppose works of art might be a very appropriate form. I can easily see it being extended to every type of investment. It would be very hard to imagine drawing a line between one type of property and another. That would not make too much sense.

COMMISSIONER PERRY: You accept the facts the time period is likely to create certainty on both sides of the line. A good many people don't think that way. They think once you are beyond the line you are safe. They won't draw the inference that if you are

short of the line you are also taxable.

MR. GIBSON: I don't know we feel this is desirable. Mr. Graham feels that a tax system of this sort with a time limit put into the law there should be an opportunity to discharge the onus that would then be placed on the taxpayer if the gain was a result of a trading venture out of pure speculation or investment.

THE CHAIRMAN: You suggest that such a tax would have a dampening effect on incentive in Canada and the development of the nation. It has been argued to the contrary that it might result in being able to duck losses.

This country is not generally accused of being full of risk-takers and common stock buyers. I wonder if there is anything in the argument that a capital gains tax might encourage risk-taking rather than dampening it. Do you think so?

MR. GIBSON: There might be. I am inclined to doubt it for two reasons.

One, it seems to me that a capital gains tax that provided completely comparable relief for losses comparable to the potential tax on gains would not be a producer of significant revenue. There is a problem unless there is some way of overcoming the problem of restricting the incidence of tax to realized gains or losses. If one does not accept the philosophy that appreciation itself should give rise to liability the taxpayer is put in the position of choosing as against the revenue if he suffers loss in respect of certain assets he may realize on then and if adequate

compensation is in fact given the revenue is likely to be the lesser and appreciated property retained for very lengthy periods. This we also feel has the unfortunate tendency to restrict the taxpayer's choice in making disposals.

Our real feeling is if proper provision is not made for losses then the taxpayer is not facing an investment in a speculative venture with a fair game ahead of him. If he loses he may or may not recover anything. If he does it will be at the lower scale of his tax rates. There is no question, however, if he had a gain he would be clearly taxable and immediately, not waiting until another period when he might have something to offset his loss. This would be very discouraging. On the other hand if a comparable provision were made for compensation for losses, 25 per cent capital gains tax and 25 per cent refund in respect of losses, this would be extremely encouraging to those who were inclined to risk their capital but I suspect it would be so hopeless from the point of view of revenue, it would be quite unacceptable.

THE CHAIRMAN: Why do you say that? Gains surely must be more than losses or people would not speculate.

MR. GIBSON: I think very sizeable gains are not realized quickly. Huge gains by corporations often form the basis for their future income-producing endeavours. The very substantial losses that are incurred in small bits and pieces would quite quickly become important.

THE CHAIRMAN: You might have to extend the

tax to unrealized gains.

MR. GIBSON: This horrible thought tempts us to believe this is a poor form of tax. The very idea that one should attempt might be very helpful to the I.B.M. type of operation but extremely difficult in the matter of reporting and the problems of evaluation and so on. It would be very difficult.

THE CHAIRMAN: I would think so. It would be something like a net worth tax.

MR. GIBSON: One would have to have regard to the liquidity, differences in liquidity of different forms of investment.

COMMISSIONER PERRY: I notice at one point the possible implication such a tax would have for corporate surpluses. Have you considered the argument that a tax on the gain reflecting the increment of money within the corporation would be a fair price to pay for the advantage of postponing the tax that would be otherwise be payable on that corporate surplus.

MR. GIBSON: I don't think we have in fact considered that argument. I am sorry, I am perhaps deviating from your question. It did occur to me there is one point that we failed to make but it comes up in connection with the capital gains realized by corporations. In the general system of taxing capital gains it gives rise to a pretty serious problem from an equitable point of view, at least in connection with capital gains realized or accruing in corporate hands. The difficulty being to avoid duplication of tax both in the hands of the shareholder and in the hands of the corporation

on a gain that is ultimately realized by the corporation.

If the assets of the corporation are appreciated the individual may sell and realize a capital gain and pay tax. The corporation itself on disposing of the assets would have a capital gains tax unless a complicated provision is made to protect against that. Taxing capital gains in the hands of the corporations, I suppose it might in a way be quid pro quo or might not be. It would not be acceptable from that point of view if individual shareholders as corporations were not also taxed on capital gains.

COMMISSIONER PERRY: I was thinking of the American system as it more or less is. It is the individual shareholder who bears the main burden of the capital gains tax. Some people do support this as a fair price to pay for the tax postponement which is allowed through the accumulation of corporate surplus on his behalf.

MR. GIBSON: I think there is a great deal in many of the arguments as to the equity or apparent fair-play nature of capital gains tax. Certainly taxpayers who are paying a heavy tax on earned income are inclined to feel that they are paying more than their share when they hear of or see taxpayers, other persons not paying any tax on substantial gains. I think the Board feels this is largely unwarranted but there is a real problem in this area.

COMMISSIONER PERRY: I think this is where you come closest to getting a tax on some real income earned somewhere that is being withheld.

MR. GIBSON: And the real beneficiary of the income. There is a difficulty in trying to do this without giving rise to other inequalities and what we feel are seriously dampening effects on the economy and at the same time producing some net revenue for the country.

I think it would be quite serious. Again you would have to have some release for distributions of income when they actually do occur which would perhaps be received by different taxpayers. I suppose distributions of income representative of this sort should be completely free of tax.

Another objection is individuals who would be tempted then to retain indefinetely their holdings and attempt to pass them on to heirs without tax. Tax free adjustment of values at death appears to be really the only satisfactory way. I understand the United states have attempted to find some way around this, I don't know on what basis, but they have abandoned the attempt, I understand, at least for the present time.

THE CHAIRMAN: They were proposing to tax unrealized increment.

MR. GIBSON: In the hands of the beneficiary. If I am not wrong they would also, I believe, have even some credit in respect of the estate of the deceased in respect of the increment portion in the estate. This becomes almost unworkable. However, it would be necessary to be fair.

I must say I get frightened of capital gains tax every time I go to the United States because

of the complexity of their system at the present time and the difficulty of finding some way of carrying out a normal transaction without getting involved in tax that in many cases would not appear at all appropriate on reorganization of a corporation organization. At the same time I should think there is a good deal of avoidance of the spirit of the law still quite possible under their system partly because of the extreme complexity of the rules.

COMMISSIONER PERRY: I recall on one occasion being invited to Washington for two or three days to attend a meeting of the American Law Institute, which is the inner circle of the American Bar. There are only two or three hundred members and they are all top lawyers of the country.

At this time Stan Surrey was working for them in preparing suggested revisions of the Internal Revenue Code. This was at the time the whole thing was going through the mill. I sat in with them for one whole day in which he talked to them about the problems involved in applying the capital gains tax just to partnerships -- just to partnerships. He had six or seven different possible solutions for what sounded to me to be an insoluble problem.

MR. GIBSON: I suppose personalities should not be brought into this too much, at least by me. I have had discussion with people who are close to the problems of the business community in the States and they feel the approach taken by Mr. Surrey, which is highly theoretical and perhaps entirely advisable

from the equitable point of view, resulted in the most elaborate and cumbersome and really unworkable system. It is almost beyond belief what the business community appears now to have to learn and understand and wend their way through.

COMMISSIONER PERRY: What really frightened me was the problems.

MR. GIBSON: Mr. Surrey had visualized the problems in the first place but they are immense and the solutions that have been devised so far are not workable, I don't think.

THE CHAIRMAN: We will continue our search for a nice easy way of doing it! Shall we move on?

COMMISSIONER PERRY: I was wondering if they could be a little more precise in elaboration of the very last paragraph of this discussion on page 7, particularly where you say "This does appear to be an area that requires some clarification in the legislation, if only to provide some degree of certainty for tax-payers and to reduce the volume of appeals to the Courts."

As you know, there is almost no legislation on this subject at the present time and I find it difficult to think what sort of legislation you have in mind, apart from the time period test we were discussing earlier.

MR. GIBSON: Perhaps we should have been more specific. We haven't included it but we had originally intended to suggest the words 'venture in the nature of trade" be removed from the definition

of business. This I don't think we were competent to suggest and recommend. I think it perhaps is worthy of some consideration. I think those words have been employed by the Court to extend the normal or probable intended meaning of the words.

I personally suspect the words "venture in nature of trade" were intended to refer to a trading transaction, one that is commonly regarded as a trade rather than to imply all of the tests of intention and secondary intention and so on that have now been attributed to that phrase. We felt it would be better if possible to go back to a pure reference to business and the way in which it is interpreted and has been interpreted in English Courts and Canadian Courts prior to the use of the words.

Whether that would leave out gains that really should be taxed is hard to say. For that reason we didn't feel we were in a position to recommend it.

THE CHAIRMAN: If a time test were brought in those words would probably be left out.

MR. GIBSON: That was our original thought in connection with the time test, dropping out might be acceptable. If the time test were included, if the time test were imported into the Act it should be restricted to certain types of commodities and so one would move fairly cautiously into the area and not make the general application without being perfectly certain this was intended and desirable.

COMMISSIONER PERRY: It is hard to tell whether it would produce more or less litigation. The

Department would try harder than ever to make use of what words it has.

MR. GIBSON: That is really why we have left it on a weak note. We haven't got an honest and sensible solution to offer.

THE CHAIRMAN: Moving on to the high rates of individual income tax you suggest if the peak were 60 per cent instead of 80 per cent the loss of revenue would not be substantial. There are various sections in the Act which are designed, I think, to alleviate the effect of the very high rate of personal income tax, such as averaging I suppose is one and stock options is another.

I should say they get there because of high rates of tax. Would there be any others you can think of?

MR. GIBSON: In the present legislation?

THE CHAIRMAN: Yes.

MR. GIBSON: The use of the corporate form by individuals for their own personal businesses is perhaps the most common method of averaging. Certainly it has a very favourable effect on the individuals who have substantial income from businesses or any other activity and they can make use of the corporate form.

THE CHAIRMAN: You are directing our minds to the form of tax and the awkwardness of the tax by virtue of the high rate and what could be accomplished if the top rate were reduced from 80 per cent to 60 per cent. I am assuming the scale would be adjusted. That

is beside the point. We are talking about the top rate of 60 per cent at the moment and I would have thought there would not be the same need for averaging as there would be for farmers and fishermen because they would not get into the top rate.

MR. GIBSON: Probably also certain types of entertainers, people of that sort whose income fluctuates very rapidly but on averaging at a relatively low level would still require some assistance in averaging. We have suggested anybody whose income varies from year to year or over a period of years by more than some set percentage. We didn't set a percentage because we had not reached any definite conclusion what percentage might be appropriate. If the income in one year more than doubled any other year in a five-year period this substantial fluctuation, if it happened to be more than two or three thousand dollars, it could have a pretty serious effect on the rate structure for individuals.

In the lower range this would be important. By cutting off the rates at the 60 per cent level this would removed the problems. Take for instance the heavy-weight boxers who simply cannot afford to fight twice in a year.

Have you some comment, John?

MR. GRAHAM: I think we had in mind the points Mr. Gibson has mentioned and also certain professional people who have a very long period of training before they are in an income-earning position.

THE CHAIRMAN: You were speaking about the

need for averaging?

MR. GRAHAM: Yes. You have very naturally picked up the figure of 60 per cent. We did mention if one were to drop the rate to 50 per cent the cost would be $10 million, which is less than 1 per cent of the revenue presently derived from personal income tax.

We feel there is some advantage in the top personal rate approximating the corporate rate so that a particular form of organization of doing business is not benefited or penalized compared to other forms of doing business.

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There are certain individuals, particularly in the professions who are unable to employ the corporate rate. Some of them in certain areas may have very high incomes. Their incomes may be subject to very wide fluctuations, and therefore we really advance two suggestions; one, that the peak rate should be reduced, feeling that there would be very little cost to revenue, and the present rates are of a nature almost too confiscatory or vindictive; and secondly, to approximate more closely the corporation rate and the top personal rate. These were really two points, and they do hit, perhaps, not too many individuals, but certainly in some cases it does put a very heavy penalty on one whose income is fluctuating widely, or people like surgeons, for example, who may be 35 years of age before they start to earn any income, and have a relatively short period of peak earnings.

MR. GIBSON: It would appear to us, although we have not really advanced this as a solution to the surplus problem, but one of the possible solutions, a number of possible solutions to the corporate surplus problem would appear to involve some peak rate or limit of taxation of dividends from corporations.

Any such limitation would only appear really appropriate if the peak rate of personal income tax were lowered to something approximating the total or top rate of tax that an individual would realize if he had his income first earned by a corporation, and then received it back; otherwise persons who were in a position to have their affairs handled through a

corporation would have a substantial advantage over those who did not.

THE CHAIRMAN: The reason you state that is I think because income which is subject to a high marginal rate if left in a corporation would be subject to tax at a lower rate than could be realized by breaking up the corporation.

MR. GIBSON: Yes.

THE CHAIRMAN: Providing the taxing break-up of the corporation was below his marginal tax rate.

MR. GIBSON: Yes, but if, for example, a ten or fifteen per cent rate were applied to dividends on corporations, a ceiling would be placed on dividends from corporations. The combined rate of tax would be in the order of -- the peak rate of tax paid after distribution would be not much less than 60 per cent.

This would make I would think the rates in excess of 60 per cent on individual incomes quite inappropriate. It would certainly appear to be so. I would think most professional bodies would have to re-consider their co-efficient on corporation tax.

THE CHAIRMAN: Are you not putting undue stress on that? What you say is, of course, quite correct. A person with a high marginal rate would be better off leaving it in a corporation, but indeed all corporations have more than one person in them, and very seldom have they all top marginal rates.

The man lower down the scale would be at a disadvantage where the man at the top of the scale would be at an advantage.

Unless the difference between the combined corporate rate and the individual top rate is very wide, I am not sure that there would be sufficient non-corporate earnings to warrant --

MR. GIBSON: I was really advancing this point as a subsidiary advantage of lowering the peak rate to something approximating top corporate rate -- in the way of solution of this corporate surplus problem, along the lines of a flat rate tax on dividends. That is really all I had in mind. This really is an incidental advantage I would think to the lowering of peak rates of tax.

COMMISSIONER WALLS: Going back to your suggestion dealing with averaging, you mentioned the use of a balance similar to that used for farmers and fishermen. There is a restriction, of course, on farmers and fishermen that might not make that applicable to the people you want to cover in that they have to be employed continuously in the same occupation for four years previous to the year of making up the tax return.

Now, that would apply very well to the professional people mentioned by Mr. Graham, but it would not apply to entertainers and inventors and many other classifications of people who get windfalls in one year.

MR. GIBSON: This is quite correct. Our submission was that it would be desirable to have averaging for reasons of the sort we contemplate generally available to all taxpayers no matter what the source of their income. Of course farmers and fishermen are

entitled to average with respect to any five-year period without regard to where the size or amount of deviation occurred in their income during that period.

This I think would be quite inappropriate. Administrative problems would be immense, but if provisions of this sort were made generally applicable with certain restrictions so that it would only apply where real need arose and where a substantial change took place in the size of income from one year to another, I think it would be so generally applicable to give very wide administrative problems.

THE CHAIRMAN: I would have thought if one reduced the marginal rate as suggested by you and with the special treatment of stock options and they could be subject to ordinary laws, whatever that may be—the cost of stock options generally falls on the shareholders rather than on the company, and it is rather a loose form of remuneration I would think.

MR. GIBSON: I would be inclined to think still it is proper to provide some sort of relief in respect of stock options. Unless the corporation is itself entitled to a deduction in respect to the option or the benefit granted, as I believe it is the case in the United States.

If an option is granted in the United States, and gives rise to ordinary income in the hands of the recipient because he disposes of his option within the prescribed period, then the corporation is, I believe, entitled to a deduction in respect to the amount that was taxable in the hands of the employee.

However, if it is to be regarded as effective distribution by a corporation, by reason I suppose of having failed to sell its stock for the full amount it could have received, then one would think something lower than the normal rates of tax should apply to the recipient. Otherwise this form of remuneration would be less popular than it is to-day.

THE CHAIRMAN: Yes, it would become less popular, but I am suggesting to you the only reason for its popularity is the high marginal rate of tax; otherwise it should fall in the same scheme as all other citizens are taxed.

MR. GIBSON: I think it is hard to be sure to what extent taxes have been a factor. Obviously they have been an important factor in these things, but I think corporations do generally feel that stock options have a beneficial effect in encouraging employees to stay with the corporation. Often they are subject to restrictions as to the period within which they can be exercised, and whether or not the employees go with the company.

I think there is some economic and business purpose for stock options, although I am perfectly sure in other cases it is not more than a means of remunerating the employee cheaply.

THE CHAIRMAN: Of course where it is a means of remunerating the employee cheaply, he should be taxed the same as the rest of us are taxed, whereas the man who is provided with stock so he will have an interest in the company, he would, if taxed in the ordinary way,

only be subject to such tax if he turned that over quickly. If he continued to hold it as an investment, which is very often the purpose of the company issuing the option; to secure the continuing interest of their officers in the company, then he would not be taxed.

MR. GIBSON: No, not under the U.S. system.

COMMISSIONER PERRY: I would think under our system, because it would then become, without special legislation, it would not be taxed because it would then become real capital gain, would it not?

MR. GIBSON: I suppose so.

COMMISSIONER PERRY: One of the confusing aspects of tax minimization in its most refined form, it is not a matter of avoiding 80 per cent tax; it is usually a matter of avoiding 16 per cent or 20 per cent tax and paying no tax at all, and it would seem even this degree of advantage leads to what your own Chairman of to-day has described as waste of talents in this area. Is this not a fact?

MR. GIBSON: I think that is true. I think relatively modest rates of tax have led to avoidance and exploiting of the method of carrying out one's affairs that give rise to paying no tax.

COMMISSIONER PERRY: How low do we have to go?

MR. GIBSON: I must say personally I am quite alarmed at the number of people who have been suggesting a 15 per cent rate in respect to dividends. I am a little inclined to think that 5 per cent is too high to be acceptable nowadays, but I think 10 per cent

seems to me to be a rate that is likely to be accepted, but I am nervous about 15 per cent as a solution to our problem.

THE CHAIRMAN: As a rate on what?

MR. GIBSON: As a ceiling on corporate distribution. I have heard a number of submissions have been made recommending 15 per cent.

THE CHAIRMAN: As flat tax on distribution.

MR. GIBSON: Yes.

COMMISSIONER WALLS: I am always concerned about other people's concern for this 80 per cent bracket. It appears people in the 80 per cent bracket are really only paying in the 60 per cent bracket because no salaried people that I know of are in that classification. With the 20 per cent dividend tax credit, the 80 per cent group, who almost entirely rely on investment income, pay only on the basis of 60 per cent.

There may be people within the normal range of 60-80 that would benefit, but I cannot see there is any great benefit to the people in the 80 per cent bracket itself.

MR. GIBSON: We take the opposite view, the real purpose being to serve in fact other than to discourage people -- it possibly has a discouraging effect on attracting people to further effort and so on. I am not really sure but I suspect there is something of that kind, but it is hard to imagine what real purposes are served by rates as high as this, as it appears to people who are subjected to them, to be

excessive.

MR. GRAHAM: Our comment is directed not only to those who are subjected to peak rates of 80 per cent, but to those who are subjected to peak rates of the higher level of 60 per cent which comes in at $60,000.00.

COMMISSIONER WALLS: That is right.

MR. GRAHAM: And although politically one probably could have few tears for those in the 80 per cent bracket, at the same time there seems to us to be no good reason for these excessively high rates.

The resulting revenue is very small, and we do seem to be inhibiting capital formation and the more useful applications of these funds than merely handing them over to the Minister of National Revenue.

COMMISSIONER WALLS: In most other countries do they not also have equally high rates? It is done for political acceptance by the working people.

MR. GRAHAM: These aspects are surely not the prime concern of the Commission, and these peak rates were usually imported under the duress of War when there were other limitations on the receipt and enjoyment of income, and they have not been removed.

THE CHAIRMAN: Most countries I have seen do not have high tax rates, but the United States and the United Kingdom do.

COMMISSIONER WALLS: That is what I was thinking.

THE CHAIRMAN: European countries generally do not, but they collect an awful lot on personal income tax. You have not suggested a proportionate rate of

tax in respect of graduated rates, and you must have debated that in your Committee. There has been a good deal said about it. Would your reason be that you believe that the use of proportionate income taxation would produce a regressive result throughout? Did you discuss this?

MR. GIBSON: We did not discuss it at any length. I think it was referred to at one of our meetings. I think generally the feeling of the Tax Committee was they do accept the principle of ability to pay, and the rough and ready way in which income may be appropriated is ability to pay. I do not think I can say we discussed this at any length.

MR. GRAHAM: The point was raised, but there was no serious advocation of it.

THE CHAIRMAN: Thank you. Corporation taxation. I think it is generally thought by Canadian taxpayers it would be a good idea if Canadian rates on corporate income were less than those in the U.S., but I am not altogether clear what the reason for that is, and I do not know that you have made a very strong case for reducing the rates below those prevailing in the United States. Would you like to add anything?

MR. GIBSON: Yes. I do not believe the Board advocates corporation rates substantially lower than those in the United States. We are most anxious that the rates not be ever allowed to exceed the U.S. rates, and in view of our withholding tax situation at the present time, we feel corporation rates should be a good deal lower than the statutory U.S. rate if U.S.

investors are to be attracted to this country.

Whether this is really what we want to do or not, I am not sure, but at the moment a U.S. corporation that may already have a subsidiary in this country or that may be contemplating establishing manufacturing facilities in Canada rather than importing goods that are manufactured in the States are not likely to be encouraged to do so if our rates are in the aggregate -- if the rate of tax would suffer here or it would be more than their own rates. This is going to discourage investment in Canada, other things being equal.

However, we feel that other things are not entirely equal; certainly on the broad picture the U.S. has many advantages, and the one we cite is the substantial market, much larger market than we have, home market, and this kind of advantage that the U.S. industry has over Canada would have to be compensated to some extent.

There may be instances where Canada has an advantage through close access to natural resources or something of that sort, but in a broad sort of way we feel that if anything the Canadian rate should be somewhat lower than the U.S. rate in order to make investment in this country as opposed to the U.S. somewhat more attractive.

THE CHAIRMAN: What are you speaking of when you speak of Canadian rates and U.S. rates? Are you speaking about the combined rates of tax on earnings of Canadian companies and withholding tax on the distribution of those earnings? Are you speaking about what

one is inclined to suggest in Canada as about 59 per cent at the present time?

MR. GIBSON: No, I am afraid we did mix the two arguments or at least the two points together a little bit. Generally we are speaking of normal tax rates, corporation taxes that will fall on a corporation both provincially and federally, compared to similar rates of tax paid by U.S. corporations to the State and Federal Government.

The effect of our withholding tax system at the present time is largely a matter of whether U.S. investment is likely to flow into this country or whether it is not. Our concern really stems from the fact that U.S. appear to be heading into a much lower corporation rate than they presently have, and our feeling is if the Canadian rate remains at a higher level in the long run those rates will have to be borne either through different prices or higher yield, and it will become harder for any investor to invest in Canadian industry.

THE CHAIRMAN: Some statements have been made having regard to the U.S. corporate investor looking at this country as a place to build a plant, and he will at the present time regard the Canadian tax rate as 52 per cent, and probably not have much regard to the lowering of tax.

In addition to that he will take withholding tax and apply it to the balance of earnings, 48 per cent, or roughly 71 per cent tax, and he will compare the 59 per cent Canadian tax rate with the rate of

his own country, roughly 52 per cent.

It has been said to us that the rates in Canada should aggregate not more than corporate tax rate in the States, so that he is at no disadvantage with regard to his Canadian investment.

On the other hand, you are saying to us if we bring our corporate earning rate in line with the U.S. rate, we can forget about withholding tax because he is not necessarily going to withdraw the profits, and leave them in Canada, and make an investment.

MR. GIBSON: I was not regarding withholding tax as the most important element in this thing. I frankly think that withholding taxes are in many, many cases -- certainly in major cases -- not an important factor in the U.S. decision, the decision of a U.S. parent company investing in Canada.

They may have an important effect on the inflow of portfolio, although in many cases taxes imposed in this way would be available for credit and full offset against taxes paid by the recipient.

However, I do think that the high rates of withholding tax are damaging, although not very seriously; in a great many of the important investments, other than perhaps from a psychological point of view.

Most U.S. investors appear to find one way or another of avoiding being taxed higher than the 52 per cent rates on profits generated in Canada either through arranging interest payments to be made or merging low tax interest with high tax dividends or

payments, or something of that sort. I personally feel high withholding rate s have more of an effect of cutting down corporation taxes that Canada, both Federal and Provincial Governments collect, than they have in discouraging certainly large U.S. parent companies from investing in this country. I think high corporate rates themselves are likely to be more important.

COMMISSIONER PERRY: We were told the possibility of merging foreign forms of income from abroad no longer existed. The right has been withdrawn.

MR. GIBSON: I think this is incorrect.

COMMISSIONER PERRY: These were fairly well versed people.

MR. GIBSON: I should then say with respect --

COMMISSIONER PERRY: They might even have been some of your clients.

MR. GIBSON: One very important method of merging or offseting one high rate of tax against a low rate of tax has been proved, and that was it is now no longer possible for a U.S. taxpayer to invest in short-term interest-bearing securities. That was the primary form of investment of this kind, and the U.S. taxpayer would, instead of investing in short-term U.S. securities, invest in short-term Canadian bank funds. This generated income against which he could apply high excessive foreign taxes that were imposed on other forms of income.

However, there are quite a number of other possible methods or other types of foreign source income that can be used in this way such as interest from

a subsidiary company or royalties received from a subsidiary company. I think they are probably the most important areas for what you might call avoidance of withholding tax.

COMMISSIONER PERRY: I put it to a group the other day that this comparison of the corporate tax rates was not quite as bad as it looked when you took into account the Canadian rate, 3 per cent, which included old age security, and if you work this out as having its counter-part in different form in the States, and add into the American 48 per cent rate something for State taxes, then the two rates are really not very far apart. In fact, the Canadian rate may be lower still.

MR. GIBSON: I would agree with Mr. Perry that it is very difficult to come up with a precise answer. You have to know the state of origin and the province in which the people do business, and everything else.

COMMISSIONER PERRY: There would not be a chasm between the rates even with the lower rates.

MR. GIBSON: I think it would have a psychological effect where our industry would truly be burdened more heavily than the U.S. industry.

COMMISSIONER PERRY: This is just an instance of the fallacies of comparing flat corporate tax rates. We find in Germany, for example, there is a capital tax which works out to equivalent of about 10 per cent corporate profit tax.

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MR. GRAHAM: Our main point, Mr. Chairman and Commissioners, was that we in Canada must be alert to the possibility of the tax proposals that have been advocated by the U.S. administration being enacted into the law and resulting in lower effective rate in the United States and in Canada; we must always have as a governing principle, if we are to encourage in any way American investment in Canada, the fact that at the most ours should not exceed theirs.

I think this was developed during the past month when the Kennedy tax proposals were very much before us.

COMMISSIONER PERRY: That is quite an acceptable and sensible statement. I am reacting a little bit, I guess, to some newspaper editorials that we are on the brink of disaster.

MR. GIBSON: I am delighted to have my statement so categorized!

I think if our rates were substantially lower than theirs this would be a foolish thing. U.S. investment in the country would be affected.

THE CHAIRMAN: The 30 per cent U.S. withholding tax.

MR. GIBSON: The very prospect of that for any industries that have investment in the United States is appalling, particularly in view of the method of dealing with income from dividends. I should think if we are to be faced with that we should give some consideration to permitting Canadian parent companies to take into account dividends in much the same way as the

United States companies do so they may be in a position to apply the high effective rate on tax dividend income. At least this would give some of the companies an opportunity to escape --

THE CHAIRMAN: Pass the high tax on to the Canadian company.

MR. GIBSON: I think it would not really have that effect. The large Canadian companies with big United States subsidiaries may, in any event, have relatively low U.S. tax on the entire income generated in the States, part which may come back in interest and royalty payments and dividend payments.

Our present system gives no relief from the high tax on dividends, against the Canadian tax paid on interest and royalty payments and dividends.

THE CHAIRMAN: You would permit polling in the same way as it is done in the United States.

MR. GIBSON: If we couldn't avoid it by getting back to the lower 5 per cent rate.

THE CHAIRMAN: How far down would we have to reduce our corporation tax in order to achieve some measure as a cure for what you pose as the difficulty of co-operative and provincially-owned enterprises? Any thoughts on that?

MR. GIBSON: What level?

THE CHAIRMAN: How far do you think it would be necessary to reduce corporation taxes in order to meet the alleged problem of Co-operatives and Provincially-owned enterprises? It would seem to me Provincially-owned enterprises are not taxed at all and

therefore one would have to reduce the corporation tax a long way.

MR. GIBSON: I don't think we were thinking of a cure. We don't visualize there is a cure entirely, but the lowering of the rate on tax imposed on normal corporations, possibly at the expense of shifting of the burden of sales tax, and there would be an improvement, not that it would cure the problem completely.

THE CHAIRMAN: As for Co-operatives, you are, I suppose, aware that they distribute all of their income and very largely that income is fully taxed in the hands of the recipients. It is not with regard to consumer goods received by a consumer but most of our products are producer goods and as such are fully taxed.

MR. GIBSON: I think we accept this. At least theoretically it answers the problem. We do think -- I don't know what sound theory is behind it -- the double taxation system on corporation profit, if there is justification for it, (a) it probably is an expediency, a very simple and effective method of collecting large amounts of revenue; and (b) society does provide a satisfactory means through the corporate form of carrying on business and there are advantages that can be obtained by carrying on business in a corporate form.

It is a very suitable form to carry on activities and Co-operatives have most of those advantages without being penalized, to the extent it is a penalty, by the double taxation system.

I find the theoretical arguments both in favour and against the co-operative treatment extremely difficult.

THE CHAIRMAN: It is very difficult indeed. It would be no cure to offer businesses the same privilege as Co-operatives with the same penalty that is required that they distribute all income and they would only be taxed once. They would not accept that.

MR. GIBSON: I don't know whether they would or not. We as a Board have not taken any stand in connection with Co-operatives. We don't feel we have the answer to it. We recognize they do appear to represent pretty severe competition to industry taxed in different ways.

THE CHAIRMAN: It is a difficult problem and you have brought it in. I wanted to know what if any views you had.

MR. GIBSON: Nothing more than a reduction in the rates applied to corporate profits would help to alleviate the problems.

THE CHAIRMAN: Thank you.

MR. CRYSLER: While it is not in our brief

2 I do think we could help you this much. In discussion, as I recall it, I may stand subject to correction, our principle point was that the main advantage a Co-operative derived was in the formation of new capital.

They have certain internal arrangements under which, as you are probably fully seized, they retain capitals. Now it is quite true that is treated as income in the hands of the member. Against that the

corporation has no option, 52 cents on the dollar is taken in tax and contributions.

THE CHAIRMAN: That is an argument put before us quite often. I cannot speak for your Board but I presume it is the same argument.

MR. CRYSLER: It is one of those points that we are not formally advocating. It did enter largely into the discussion.

THE CHAIRMAN: We will break now for ten minutes and continue at Page 13.

---A short adjournment.

THE CHAIRMAN: We are starting at the next section which is at the top of Page 13 "Split Corporate Rate of Tax - Associated Corporations".

You indicate you are in favour of doing away with the split. You say "Alternatively, if a two-rate structure is to be maintained, the present control tests could be supplemented by a separate kind of business test as presently used in the U.S."

I don't know what that separate kind of business test is. I have had a search made which indicated three or four tests in the United States. What is it that you have in mind with regard to the other test that might be added?

MR. GIBSON: I first of all should apologize for not being better prepared to answer the question. It was suggested to us by one of the members of the Committee that the United States do have a test that turns on the nature of the business conducted by separate corporations.

In our discussions we had discussed the possibility of introducing a provision that would permit corporations that were subject to common control to avoid being regarded as associated companies that have to share the low rate of tax and if the businesses conducted by the two companies were distinct and different and there were not substantial inter-company transactions between the two --

THE CHAIRMAN: If there were not an economic relationship.

MR. GIBSON: That is a very much better way of putting it.

THE CHAIRMAN: I don't know how you define economic relationship.

MR. GIBSON: We were not being very specific in our thinking on the thing other than using the rather simple examples of the boot and shoe business and the grocery business. Obviously the problems of defining the differences and distinctions between businesses would be much more difficult.

THE CHAIRMAN: When you move the law into the realm of economic distinctions you have to provide for discretion at that point.

Do you think the law can be written so as to distinguish or provide a test which would be suitable for the economic nature of the businesses?

MR. GIBSON: This is a real problem, I think, in an area of this particular kind. The Board has always been very opposed to the use of discretionary power in the hands of administration, particularly where it can

be exercised at a level below that of elected officials.

Our basic concern there is wherever discretion is resorted to it is generally because it has been difficult to establish the principles on which one is expected to apply the discretion. Where it is possible to identify and clearly set up a set of principles on which distinctions are to be made then it should presumably be possible to express those in words which are acceptable of reasonable interpretation by the Courts. Certainly we would hope this would be the case.

One of the major problems in the split corporation rate of tax is there are not clear principles that are evident to the population at large or the Courts that govern the reason for the rules as they are. Were it possible to define in a sensible sort of way and explain the principles that lie behind continuing the low rate in certain circumstances and granting it in others I think it would then be possible to establish rules that would be of a more general nature and that would be capable of proper administration and interpretation by the Courts.

I think we feel at the present time there is not a clear and underlying philosophy that makes sense lying behind the split rate of tax.

In part it could be improved at least in certain cases by permitting the low rate for new businesses without regard to whether they happen to be controlled by the same person who controls some completely different and separate businesses. That would seem to us to be an improvement but it would not really solve the problem.

The real problem seems to be how does one define "small" in connection with a business.

THE CHAIRMAN: "Small" is only one word. The context says "small", "associated", also "economic relationship". Those are the three things you state, I think. Most tax laws do distinguish between private and public companies with in some way different taxation applied to each. We have been successful so far in avoiding such distinction in our tax laws but other laws do make such a distinction.

Maybe our tax laws should be directed to that because it is often said that a small business is generally less profitable than a large business and needs encouragement and needs help. If that is true, we should be able to distinguish the one from the other and apply such encouragement.

MR. GIBSON: Obviously one of the main purposes would appear to be to remove what would be a serious impediment to small businesses and adopt the corporate form and take advantage of the flexibility of interest that is available through incorporation.

If small businesses were subject to the 50 per cent tax rate on all the profits generated without any relief at all, even though the owners of the business had very small incomes, unless there were extremely flexible rules about the deductibility of small payments for example, it would work serious hardship. This I think we recognize and we feel if the split rate is to be abandoned something must be done to protect and make it possible for a small owner to use the corporate form,

possibly through the optional use of a personal corporation type of payment.

THE CHAIRMAN: I don't think it is very hard to devise something for them. The main difficulty is to put them in a separate class so we know what we are talking about.

MR. GIBSON: That is quite true.

COMMISSIONER WALLS: I think it should be drawn to your attention that our research staff don't agree with you on the figures of the 37 per cent giving 7 million more than taken at the present time. They feel that you have overlooked the Provincial ~~form~~ and other tax credits and actually it would have to be 43 per cent to give that return.

MR. GIBSON: This I think proves the merit of our decision not to rely too heavily on statistics that we ourselves produce. I apologize if these are inaccurate.

THE CHAIRMAN: I would not be very much concerned. I am going to query the staff on the 43 per cent. I saw something the other day which made me think it was 47 per cent.

COMMISSIONER PERRY: It is just as well not to get confused with arithmetic.

MR. CRYSLER: Could I offer you our assurance that we will look over the figures and let you know just how we did make them up. We will let your research gentleman know how we made up the figures so the problem can be easily resolved.

COMMISSIONER WALLS: I presume you will also supply the research staff with your figures, Mr. Chairman!

THE CHAIRMAN: Is there anything further on this split rate? We will move on to Corporate Surplus.

You suggest "that dividends received by one company from another out of designated surplus would continue to enjoy exemption so long as the distribution would not result in the effective disappearance of undistributed income". Designated surplus was really, I think, established in the Act so one is not in a position of buying a company with a lot of assets and using the assets of the company to pay the purchase price. One could still accomplish that under your proposal, I think.

MR. GIBSON: We felt probably not. We haven't explored this as far as we perhaps should in making it a positive recommendation. We have advanced it because it is a proposal that has been considered and advocated by the Board previously as a general proposition and because we are not aware of anybody else advancing this same proposition. We don't do so quite as formally as we might.

I think all on the Board feel a clean sweep could be made in a very satisfactory way with a completely new method and this would be desirable. We did, however, feel it was worthwhile bringing this proposal forward again. On this point if the proposal were to be carried out the illustration we have in mind is an individual who owns the shares of a corporation and may form a holding company to sell his shares to the holding company and taking back preference shares of the holding company in exchange and subsequently redeeming a debt out of dividends

withdrawn from the subsidiary company.

Under our proposal we believe if the principles underlying 105C were applied to this situation this situation would result in effective withdrawal of assets. The assets of the two companies taken together would no longer be adequate to represent the undistributed income.

If it did not occur the tax should not fall. This is the guts of the proposal we put forward. Now whether it is entirely workable or would leave a good many complexities in the existing law I don't know. As a principle it appealed to us as something based on fairly sound theory.

THE CHAIRMAN: Assets withdrawn are frequently replaced by simple debt, by the shareholder using the assets --

MR. GIBSON: By loan to the shareholder.

THE CHAIRMAN: Yes, even though perhaps prohibited under other laws. I think there are ways to circumvent the other laws. It would seem to me you don't cure anything unless you recognize when assets are withdrawn in that way there is a diminution in the combined surplus.

MR. GIBSON: I am not personally sure this is so. I think it would perhaps depend more on the loan. If the loan were made to a shareholder and was an adequately and properly secured loan and was something that was normal in the sense that it might as easily have occurred between people dealing at arms length the same sort of tests are already contained in the law.

I suppose if the possibility that shareholders

would exploit their position to take loans from a corporation, if that was regarded as serious the existing rules that apply in those circumstances could be continued.

THE CHAIRMAN: I am sure they exploit their position to take full advantage of the law. That is their duty so to do. It seems to me that one of the loopholes in the present scheme is pools of surplus left all over the place not supported by assets of any substance.

The cure is provided in most other countries with some form of deemed distribution tax. I would have thought that would have been necessary under what you propose here.

MR. GIBSON: This is really what we do propose wherever a transaction occurs that results in a company no longer having assets of value that represent the undistributed income on hand at that time. At the time that situation occurs the tax would be imposed at a level which is comparable to rates of tax applicable to others.

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THE CHAIRMAN: That requires judgment as to the value.

MR. GIBSON: Yes, and that of course is one of the major obstacles in this sort of a proposal.

THE CHAIRMAN: Deemed distribution taxes are difficult to impose. Most countries I think use them very seldom.

MR. GIBSON: Yes. It perhaps is not quite so serious an objection in view of the fact that in the vast majority of cases distribution will either be taxable or not taxable. It would only be in borderline areas where a graduation will be required. I would imagine that the administration would be in a position to refrain from applying its powers under this sort of provision in cases where it was very close to the borderline.

THE CHAIRMAN: You are passing something pretty close to discretion over the administration of these matters -- presumably with suitable checks -- but it is still quite an area where discretion would have to be exercised in the first instance.

MR. GIBSON: Yes, I think that is true.

THE CHAIRMAN: Your next comment I found interesting. Old Age Security Tax Paid By Corporations. I believe this is the first time that has been brought to our attention, with non-tax-paying groups, and the employees receive the benefit of this.

COMMISSIONER WALLS: You don't state just how you are going to collect this, whether you are going to make it an addition to other taxes, and if so, which other taxes?

MR. GRAHAM: Mr. Chairman and Mr. Walls, whether the old age security tax should be more properly characterized as a payroll tax as it is in certain jurisdictions, it did seem to the Board that it was unfair that a fund which ostensably is supported by employees and employers, and to some extent by the general public, should have one leg of the three-legged stool so shortened by reason of the fact that it is based on income tax liability and a very substantial number of employers consequently make no contribution towards the old age security pension of their employees.

COMMISSIONER WALLS: Basically, to correct that you feel that income tax would be a most logical tax?

MR. GRAHAM: Payroll tax.

MR. GIBSON: Or possibly eleminating the third leg; having a two-legged stool. Not that that is a very good analogy.

COMMISSIONER WALLS: I think you had better go easy on that. It seems to me you are unloading an awful lot on another of these legs that you will be coming to in a minute.

MR. GRAHAM: We conceived our primary function was to point out what we regarded as an inequity in the present arrangement, and a very substantial competitive advantage or disadvantage enjoyed and suffered by certain employing taxpayers.

We do not recommend specifically which way it should go. However, speaking personally, payroll tax is a very obvious answer that occurs immediately if

one is to have contributions from the employer as well as the employee.

THE CHAIRMAN: What countries have payroll taxes for this purpose? The United States?

MR. GRAHAM: I believe the United States. Yes, the United States have.

COMMISSIONER PERRY: Australia has payroll tax.

MR. GIBSON: I speak subject to correction. I am almost certain Great Britain has in connection with public retirement schemes. Also, Mr. Perry, you mentioned in examining our Canadian overall corporate rate, one does have to recognize the fact that other countries have payroll taxes. I thought that point is well taken. It draws attention to the point we are making here, that 2 per cent tax on corporate profits is in a way related to the amount of payroll, and does not fall on many people that have payrolls, so it is not exactly a comparable form of taxation.

It may be a good deal less in some cases on Canadian corporations than would be imposed if it was on payroll.

THE CHAIRMAN: You think it should be proportionate to the labour intensity of the particular business?

MR. GIBSON: I am not sure we have reached a conclusion on that.

MR. GRAHAM: We do feel this, Mr. Chairman, it might well be that the rate may be lowered and reduce the revenue required to support the fund.

THE CHAIRMAN: The base would be broader?

MR. GRAHAM: The base would be so much broader that the rate could in fact be lowered. That would seem to follow in a logical sequence. If this is only now producing some 16 per cent of the revenue of the fund, if it was broader based, there could be a lower percentage take from employees and from those employers who are presently paying through corporate income tax.

COMMISSIONER GRANT: Payroll deduction is contemplated in the proposed pension plan which is under consideration now?

MR. GRAHAM: My understanding of the proposals as announced on the 16th of July by the Honourable Miss LaMarsh was that employers are required to pay not less than 50 per cent. The employees may or may not pay up to 50 per cent, and that is based on compensation, and therefore really a payroll tax up to $4,000.00.

COMMISSIONER GRANT: It is contemplated a rate of 2 per cent.

MR. GRAHAM: Not more than 2 per cent in total for the first ten years.

COMMISSIONER WALLS: Alternatively to the payroll deduction, would it not be possible to make it compulsory that these non-taxable corporations pay this 3 per cent tax just the same as they pay their property tax and other taxes which they then take into consideration if they lose money like some of the Government owned corporations ~~groups~~ have lost money? This is for a service. Could you not force them to pay this particular tax?

MR. GRAHAM: I have no doubt that it might be developed, but at the present time the language of

the statute is that every corporation liable to pay tax under Part 1 of the Income Tax Act, and therefore of course it excludes a substantial number. It also of course excludes non-corporate employers.

COMMISSIONER WALLS: That is right.

THE CHAIRMAN: And it would require a fair measure of income to impose the tax which probably would not apply in the case of some of these organizations that they are directing themselves to such as Provincial Commissions.

I would have thought they are not designed to seek income in the same way.

MR. GIBSON: One of our points really was that we are not at all satisfied that business income is a proper measure of the responsibility of those firms.

COMMISSIONER GRANT: You would have to strike a different rate for some organizations than what is being paid by the corporations which pays income because their deduction is an expense before determination of income for tax purposes.

MR. GRAHAM: If I may say, sir, we would not suggest that part of it be based on income and part otherwise. If it is a cost of doing business, it would still be deductible. In other words, if it was payroll tax or compensation it would still be deductible as an expense.

COMMISSIONER WALLS: Yes.

MR. GRAHAM: There is the point, and that is it is only corporate taxpayers, employers, that presently have to pay.

COMMISSIONER GRANT: Yes. I was thinking of the case of a non-profit organization. If they are called upon to pay 2 per cent, they would be paying that rate without any relief whatsoever, whereas the corporation, which is based on the 3 per cent rate, the shareholder does get relief from that 2 per cent.

MR. GRAHAM: That is true. At the same time, speaking for myself alone, if our old age security programme is supposed to be national in scope and supported on the broadest possible base, it does seem unfair that there should be subsidies flowing towards those who happen to spend their lives in the employ of non-profit corporations.

MR. GIBSON: I would also like to question the point made by Mr. Grant. I doubt really whether one could properly say that an expense incurred by a corporation is borne in effect by the shareholders, necessarily. If it is an expense necessarily on the earning of the income and could not be avoided, I would think most businesses would attempt to recover their expense in the selling price of their product.

This may be impossible if a form of taxation is levied in such a way that it increases the costs of production beyond the point where the costs can be recovered.

Of course, this would dry up the form of business or lower the rate of return, but I should think generally that costs cannot be said to be borne by the shareholders and therefore the only costs the corporations have.

COMMISSIONER GRANT: It seems to be a moot question.

MR. GIBSON: I think so.

COMMISSIONER GRANT: It is shared somewhere in about three different ways.

COMMISSIONER PERRY: I think you have to really consider the three taxes that are used here are simply normal devices for obtaining revenue to be used for specific purpose. One can easily visualize that there are citizens in this country who make no direct contribution to the old age security whatsoever. They are below personal income tax exemptions. Their income goes for purchasing things which are largely exempt from sales tax, and they are not working for employers who are required to pay a corporate tax rate, so that it is not a very sophisticated tax system. Simply the use of existing devices for specific purposes.

MR. GRAHAM: I would agree with that, Mr. Perry, and I would also say that one of the things that brought this to our mind was the increase from 2 per cent to 3 per cent, whichin the case of tax-paying corporations, is a fairly substantial increase. It is a one per cent increase, and it does not apply across the board to all employers. As it might well be without any inequity of any kind, this would be a method whereby one percentage point could be taken off corporation tax rates and be fully recovered from other sources, which from a philosophical standpoint it is difficult to justify their having relief from providing for the retirement of their employees.

COMMISSIONER PERRY: Yes, if you look at it segment by segment in that way I think you might build a pseudo logical case.

MR. GRAHAM: It is a hybrid base at the present time.

COMMISSIONER PERRY: It is just using the general tax for a specific purpose, and with the rather loose approach on the other two main sources, I find it difficult to see why we are worrying about making this particular one more logical.

MR. GRAHAM: It may be that the entire base of financing at the fund should be reexamined by the Commission.

MR. GIBSON: I think it is not inconsistent with the attitude we have taken towards corporation and personal rates of tax, and our suggestion that the corporation tax be reduced, and if necessary, be an expense in increased commodity tax.

THE CHAIRMAN: Moving on now to the next heading, Determination of Income, I'm interested to see that you believe that there are two principles that should be followed: generally, procedures which conform with accepted accounting and business practices should be acceptable for tax purposes, and (2) the methods adopted in computing income should be followed consistently from year to year.

I would like to know how far you would be prepared to go in rewriting the Act or re-writing the Section of the Act.

You will all recall that this matter was

brought up in 1948 or 1949, and at that time it was thought that accounting principles were not sufficiently well defined, to which taxation of income might be tied.

You believe that the words "according to accounting principles" -- I think you say it should be in accordance with business principles.

MR. GIBSON: I do not believe we would advocate the appropriation of specific rules of this sort particularly not one that would tie it to generally accepted accounting principles. That was not our intention, but really it is our feeling that the principles of law have gradually pulled, in certain instances, away from what would be generally commercial practice.

I think that would be a better expression in the determination of income, and it is our feeling that the normal determination of income in the eyes of a businessman is a better yardstick than what has developed gradually through case law in particular instances, in any event.

We have not by any means attempted to recite instances, many instances, of non-deductable expenses, for example, that are regarded as proper business expense that are not presently allowed as a deduction for tax purposes, partly because of the application of legal principles, stemming back from the very early days when life was somewhat more simple.

I do not think we had in mind that this should be corrected by a general statement of principle in the law as much as by correction of individual abuses.

THE CHAIRMAN: I suppose semantics are important here. Surely accounting is used to report business transactions in a form suitably understood by tax assessors and by investors. If that is the case, accounting is the language, and therefore we should use the art which is the language, should we not?

MR. GIBSON: Personally, as an accountant, I am fearful of having a rule of law which is dependent on principles that have not necessarily been clearly established and could be capable of clear definition. I rather dislike the thought of a case being waved before the Supreme Court with different accountants producing different evidence of what should be regarded as accepted accounting practice, and having the judge decide the matter.

THE CHAIRMAN: Would you sooner have a businessman recite how business transactions should be reported? I would have thought that was a job for accountants.

MR. GIBSON: I think an accountant's evidence has always been accepted as proper and useful in any question of what was a proper determination of profit for a particular business in the light of its circumstances; but to put a rule of law that related to accepted accounting practice I think is a dangerous thing.

This would have an unfavourable effect, quite frankly, on accounting practices. I am afraid the accountants might be subject to some pressure to use practices that were favourable for tax purposes, and it might not become general, but I think it would be unfortunate.

An illustration of this I think was in the days when the amounts deductible for capital cost allowances were restricted to the amounts provided for in the accounts. I personally think this was a rather unfortunate thing because it put pressure on the accounting profession to accept allowances or provisions for depreciation that were in excess of what might be the proper accounting practice of the industry.

3 THE CHAIRMAN: Do you think the use of the words "accounting of business" would make any difference? I would have thought the pressure would be exactly the same. Accounting is reporting of business.

MR. GIBSON: It may be so. I do not see how really one can adopt legal phraseology that is going to be of too much assistance in this area other than to examine particular uses or objections which one has developed over the years in the way of treating deductions as one kind or another that seem proper and sensible and are only disallowed because of precedent, in effect, rather than for any sound principle.

In attacking this, it may be possible to deal with it by introducing general statements of law that would permit deduction of all expenses that are laid out for the purposes of the trade, with certain enumerated exceptions, such as those related to purchase or acquisition of assets of a permanent nature.

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THE CHAIRMAN: As an accountant myself I have always taken pride in the fact that I think our profession has done its job very well in reporting in an objective manner on business transactions. It would seem to me that only accounting can be used to report income. There is not anything else to report income other than accounting. If that is correct, why duck the term "accounting principles".

MR. GIBSON: I think accounting principles must be applied. Obviously accounting as an art must be accepted in doing these things and it seems to me the use of accounting is merely the device of reporting on the facts more than the determining of the amount of income or profit.

I would be inclined to think that profit is something that can be determined only by the use of accounting techniques but they are not necessarily the principles that govern the determination of profit in all circumstances. I am afraid I am a little at sea in the application of accounting principles.

MR. CRYSLER: I was wondering if it would help to a better understanding of what we are driving at there if in the first place we put No. 2 first consistently. Then we follow that up by the suggestion that in determining the validity of the consistency that accepted accounting and business practices should be taken into account.

Put accounting and business practices in possession of evidence that would have to be considered.

THE CHAIRMAN: Consistency is only one matter

we are attempting to achieve. One is a proper statement. Your principle here must deal with accounting and with its consistency. You would agree with that?

MR. GRAHAM: If I as a lawyer might intervene on the interesting discussion between members of the Institute it would seem if you follow consistency too heavily you put yourself in a straight jacket and hinder development in accounting practices, which is the very thing Mr. Gibson is referring to.

THE CHAIRMAN: Any accountant knows consistency is a most difficult thing to decide upon.

MR. GRAHAM: She is known as a fickle jade!

THE CHAIRMAN: You can always make out cases for things being consistent. There are some things which appear on the surface as consistent and then three or four more tests that show it won't be consistent. That happens in almost all circumstances.

MR. GIBSON: I would suggest the main point is departure from method to determine income that is consistent in prior years should (a) be forced on taxpayers only in circumstances where it is clearly warranted; and (b) there should be, I should think, more appropriate rules for the transition from one method to another than there are at the present time.

There is quite a gap in the existing rules as to what should be done to ensure that the same income is not taxed twice or that income does not escape tax through the shifting from one method to another.

On the question of business practice, the only point that I perhaps might make is between accounting

principles and business practice it seems to me one can say the business practice is perhaps easier to identify, the accounting techniques used in connection with the particular type of business is easier to identify as general accounting principles applicable to all types of businesses.

COMMISSIONER PERRY: I think on this general discussion the experience of the British Royal Commission on Taxation of Profits on Income certainly was quite helpful and indicative.

They considered several general forms of wording and finally despaired of achieving anything through any of them as long as the existing jurisprudence stood in the way. They ended up with the recommendation that the first step that had to be taken was that several of these leading cases simply be legislated out of existence by an amendment to the statute.

No matter what words you put into the statute, judged in the very comprehensive character of these leading cases developed in a different day, you are going to end up right back where you are now.

I would think this is probably the position that we have. They are quite properly applying existing jurisprudence whereas without the jurisprudence these could be looked at in a fresh light so it may in fact not require any amendment to the existing statute at all.

MR. GIBSON: It was our feeling that Sections 12 (1) (a) and 12 (1) (b) might be reworded to give the Courts a right to take a fresh look.

COMMISSIONER PERRY: It might be necessary to take the step the British Royal Commission thought was the first step.

MR. GIBSON: It sounds like it might be a very productive step.

COMMISSIONER PERRY: I never heard of the device being employed. That is their recommendation.

MR. GIBSON: I must say I didn't quite appreciate that.

COMMISSIONER PERRY: In other words, inviting a whole new approach and forgetting the existing jurisprudence.

MR. GIBSON: That could be very productive and rather a lot of fun to go through the decisions and decide which ones.

COMMISSIONER PERRY: I imagine the list would get fairly long.

MR. CRYSLER: I thought I would raise this question. How would you expect the Court to decide in the future if you don't change the ground rules. I respectfully suggest that to merely outlaw certain decisions, which is within the power of Parliament legally, you would probably find yourself in the whole ratrace again unless you changed the ground rules.

THE CHAIRMAN: I thought that was what was implied, the ground rules would be altered.

COMMISSIONER PERRY: To me any set of words I have ever looked at could give almost any meaning you wished depending on the frame of mind you are in.

MR. GIBSON: That particular frame of mind

has some sort of permanent effect on future Courts.

COMMISSIONER PERRY: The judge, of course, is guided by past decisions just as the expression "expenditure for the purpose of the business" can be liberally interpreted or very niggardly interpreted.

THE CHAIRMAN: Going over the page I am looking at some of the items that you draw attention to. You point out instances where accounting procedures for business purposes do not accord with the manner in which business income is to be determined for tax purposes.

In Item (III) you have valuation of inventories. Did you have in mind the base stock or LIFO methods?

MR. GIBSON: I think so. I think that was what was intended here more than merely the complaint about administrative abuse or what is regarded as abuse by their attempts to alter existing practice, for example by the inclusion of some fixed overhead in inventory valuations. I think the comment is intended mainly as an objection to refusal in law to permit the use of methods that may appear appropriate for business purposes in the determination of profit.

THE CHAIRMAN: Well, of course, when it comes to inventories I question whether that can be thrown wide open. It would seem to me one can stretch an application, as is heard in the States, to a point where it becomes a tax device rather than a good measurement of income. It is so easy to erode the principle in the case of inventories that I would be very nervous

about it, wouldn't you?

MR. GIBSON: Perhaps I should be. I have never felt that the consistent application of any reasonably sensible method of determining inventories would have an undesirable effect, as long as it is consistently applied and is not wholly inappropriate I think it should be acceptable. The LIFO method seems to be sensible to employ in a situation where it is reasonably appropriate.

THE CHAIRMAN: It seems to be employed in the United States in methods which are far departed --

MR. GIBSON: I think that perhaps is so. Whether this is desirable or not I am not really competent to say. I don't know much about the extent to which it is used. I have heard of it being used in circumstances I regarded as really proper.

THE CHAIRMAN: It is used as an anti-inflation device rather than purely to measure income and if one believes that an anti-inflation device is a good thing to introduce into accounting at this time --

MR. GIBSON: Then it ought to be more generally applied than to inventories?

THE CHAIRMAN: I would think so.

MR. GIBSON: Where it is useful in eliminating mere fluctuations in the value of an inventory from year to year, a constant inventory in quantity, then I think it is much more benefit.

THE CHAIRMAN: Oh, I think so. It has been surprising to me the few suggestions that have been put to us in support of the LIFO method of valuation.

There has been one outstanding one and I don't think anything more than that, or almost nothing more. I suspect the reason is that the price level has been fairly even for a while.

MR. GIBSON: Certainly our Board has not had suggested to it many recommendations on this point. I think it is a problem for a relatively few taxpayers for whom it is most important really.

THE CHAIRMAN: We will move on to (V).5 (VI). "Taking into income of substantial amounts received for inventories and receivables which become subject to high progressive rates of tax where a taxpayer (particularly of one who has adopted a cash basis for reporting of income) disposes of his business and assets." This is a departure between business income for tax purposes and business income.

I am sorry, this does not refer to cash basis.

MR. GIBSON: Yes. Perhaps our comment here is not properly placed as being a comment in connection with the differences between accounting and business purposes. Our concern here is really for the effect on graduated rates for individuals, treatment of disposals of inventories and receivables and so on. I think the placing of this comment is not as appropriate as it might be.

COMMISSIONER GRANT: In speaking of terms of accounting procedure what bearing has the comment on inventory here on the fact that an inventory is prepared by the company and, let us say, submitted to

the auditors and as I understand it without exception, perhaps not without exception, I would think almost without exception accepted by the auditors.

THE CHAIRMAN: You might as well reply to that.

MR. GIBSON: It is a very long time since I have been called on to question the acceptability of lists supplied by one of our clients.

I am afraid, as I mentioned earlier, that the comment in connection with Item (V) disposal of inventories is not entirely applicable to the accounting principles. It has more to do with the unfairness or application of graduated rates, the circumstances where a taxpayer is required to include a very large sum of his money income for one year through the disposal inventories and so on.

THE CHAIRMAN: I think Mr. Grant is referring to item (III). I think that is well placed where it is. You are drawing a distinction between evaluation for business purposes and evaluation for tax purposes.

MR. GIBSON: Perhaps I did misunderstand the question. I thought it was referring to item (V). Accountants will and do accept in certain circumstances the method of determining inventory that is not acceptable for tax purposes under the present law. For example, Mr. Carter, has pointed out the use of the LIFO method and the base stock method for determining inventories which may be proper in a particular situation and for particular types of businesses and accepted for accounting

purposes, but are not accepted for tax purposes.

COMMISSIONER GRANT: Is it the practice for the auditor in his certificate to qualify his certificate in any way with respect to the inventory?

MR. GIBSON: I believe it is if he feels that the method chosen does not properly reflect income in accordance with the generally accepted accounting principles or does not represent a proper valuation of the assets in accordance with the proper accounting principles.

Also I think it has become much more common now to identify the method used in determining inventories more precisely than has been usual in the past in financial statements.

THE CHAIRMAN: Mr. Gibson, would you mind telling Mr. Grant it is the accountant's job to examine the inventory to the same extent as any item in the balance sheet and to take the responsibility for it.

---Laughter.

MR. GIBSON: Thank you very much for putting those words into my mouth. That is quite true.

THE CHAIRMAN: You will say "yes" to that?

MR. GIBSON: Yes.

COMMISSIONER GRANT: That is your answer?

MR. GIBSON: Yes.

COMMISSIONER GRANT: Let me follow that up by asking you how does the auditor satisfy himself the inventory is a reflection of the true position of the business?

MR. GIBSON: First of all he must satisfy

himself as to the facts that support the amounts in the inventory and that are included. Also he must determine in his own judgment whether the methods chosen for evaluating the inventory are proper under the circumstances.

COMMISSIONER GRANT: He could do that by consultation with the client and by asking them how they arrived at the figures. He doesn't do a spot check?

MR. GIBSON: Yes, it is almost a universal practice now to make physical verification of the facts.

THE CHAIRMAN: I see one of my clients sitting down there. He knows perfectly well I climb all over his inventory.

MR. TAYLOR: It is very difficult for an auditor to tell how many tons of coal we have.

MR. GIBSON: Nowadays he does his best at least to be sure there is a ton of coal or appears to be.

COMMISSIONER GRANT: For instance, if he is auditing, let us say, a retail grocery business, does he have any means of doing a spot check on the amount of stock on hand?

MR. GIBSON: This is not often done in a large organization at one time, at the balance sheet date, for example. A great deal of the auditor's responsibility depends on the adequacy of the accounting records maintained by the organization and whether the records are reliable. The reliability is often tested throughout the year on spot checks at various locations and so on. Where the reliability has been established he may feel he is entitled to accept the records at the

year end.

COMMISSIONER GRANT: Is the principle of perpetual inventories used wherever possible?

MR. GIBSON: Yes, it is. In large organizations it is very common. If it is not used it makes necessary a complete physical count at every year end to establish a proper inventory.

THE CHAIRMAN: I haven't got anything until we get to the discussion on capital cost allowance. Has anybody else anything? I think you would agree that the present system in Canada is a fairly generous system. Before one takes into consideration the special depreciation the normal basis is a generous basis and in fact demonstrated by the fact that the credit balance on a great many balance sheets is representative of what is claimed and what is entitled to using normal depreciation.

Now that being so you point out to us that there are some items inadequately depreciated under the existing system. Does not one offset the other? Are not the clauses broad enough to take care of the whole?

MR. GIBSON: I frankly don't think they are because in some industries particularly the preponderence of the assets will be of a character that does not have attributed to it a high enough rate. We have cited the electronic industry and also the leasing business as two illustrations of this sort of thing. For an entity that has various types of assets, some of which rates are too high and more than adequate, and for others less,

it should balance out. I think the Board feels that there are situations where taxpayers are unfairly penalized by the rate structure.

THE CHAIRMAN: We have had I.B.M. before us pointing out that the rates generally speaking are not adequate to take care of the obsolesence of their equipment. Do you think there are many more than that industry?

MR. GRAHAM: There are one or two others in the generic field, electronics, the broadcasting industry, that type of industry where the obsolesence factor is much more significant than the actual wearing-out factor where in order to keep pace competitively you have to do a pretty complete reinstallation perhaps over a period of every four or five years in order to keep abreast. These are unusual cases but they do exist.

The Board does not have any general complaint with respect to capital cost allowance. We did wish to point out that in certain industries obsolescence is such a substantial element it should be compensated in the rate.

As Mr. Gibson has said in the leasing business we think you have a much greater wear and tear and a much shorter life of equipment. It may be if there were some greater facility for the amending and altering of rates in appropriate cases it should be done. The whole technological field in recent years has been affected and obsolesence is affected as well as straight wearing out. I know about it in the broadcasting industry and I know of that aspect in electronics. Rates are

not adequate at 20 per cent and 25 per cent.

COMMISSIONER WALLS: We have had some evidence before us that the degree of obsolesence in the electronics business is over the crest, as it were, they have gone through a period of new development and they have reached a stage now whereby the present rate might be quite adequate in the future. Do you not think an industry would rather have a stable rate than a rate that would be fluctuating and where they would never be sure a year in advance what the rates would be.

MR. GRAHAM: I would agree with that completely, of course. The descriptive word "electronics" is almost as embracing as "manufacturing". There are different branches of the electronics industry, in the some of which undoubtedly there is now some stability but there are still branches of the electronics industry where obsolesence is still a significant factor. It may be that some special division within the clause or category would be required or desirable but I must say that broadly the Board is not dissatisfied and is making no strong representation across the board with respect to capital cost. We did confine ourselves to the two areas where we did feel there were present inequities.

MR. GIBSON: The Board is generally in favour of our system as opposed to the system in the United States where it is very much hoped to avoid the proliferation of the detail returns and so on relating to appreciable property.

THE CHAIRMAN: Ours is a good system visa

vis any system in the world.

MR. GIBSON: The system is very much to be admired, I think.

THE CHAIRMAN: The next item is Tax on Mortgage Interest Received. You have brought to us something new here. I haven't heard the suggestion that where a taxpayer is in receipt of investment income he should be allowed mortgage interest. The purpose of this would be because he does not wish to or is in no position to liquidate his other investments and pay off the mortgage, I assume, or it should not be necessary for him to arrange his affairs so as to suit the Tax Act. I would have thought that might have been offset by difficulties of assessment, but I don't know. Do you think you impose much difficulty in the way of administration or assessing?

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MR. GRAHAM: We did not think so. The recipient of the interest should be reporting it. This is what might be referred to as a homely problem, and I say that with no sense of pun. Many, many taxpayers are in this position through circumstances completely beyond their control in the selling and buying of houses.

If they do have investment income, it seems to us appropriate there should be a deduction for mortgage interest because a typical average home buyer probably sells one home and may well have to take a mortgage back; he buys another home and because he could not get all cash for the previous house, he has to put a mortgage on the new one. But there is not a market for that type of mortgage normally.

THE CHAIRMAN: You would restrict the deduction to the extent of investment income?

MR. GRAHAM: That is our submission.

THE CHAIRMAN: We have had lots of representations to the effect it should be extended to all income, and usually they point out, it seems to us, that would be fair only if there was an imputed rent.

MR. GRAHAM: We restrict ourselves entirely to what seems to us to be an incident that arises in thousands of cases every year, and it can only be offset against investment income.

This is very frequently drawn to the attention of the Board. It comes up over and over again, and while we recognize I think the political difficulties of granting a deduction for interest on mortgages paid by taxpayers who have invested income,

and not make any similar allowances for those who are in a worse condition, it is a source of irritation and frustration on the part of many people who simply cannot understand, and it seems to me that the tax system was brought into some sort of disrepute because of this.

COMMISSIONER GRANT: Do you not think this situation arises in large part due to the fact that first mortgages are restricted considerably in their amount in relation to the sale value of the property? That is to say, in the Province of Ontario I believe the maximum amount is 66 2/3. ~~two-thirds.~~

MR. GRAHAM: May I interject, Mr. Grant? I think when Mr. Gibson was referring to first mortgage and second mortgage, he was referring to mortgage A and mortgage B.

MR. GIBSON: That is right.

MR. GRAHAM: He was not referring to it in the legal sense of first charge and second charge. I think he was referring to the mortgage you are required to take back when you sell your property on which you have to pay income.

COMMISSIONER GRANT: I think this has a bearing.

MR. GRAHAM: Oh, yes, there is a factor there, sure.

COMMISSIONER GRANT: Because property values, real estate values, have soared, and a person goes out to buy a house and he is forced to lay out something in the vicinity of, let us say, $22,000.00 to $30,000.00. He seeks a mortgage. If the property is appraised at,

let us say, $25,000.00, the value of the first mortgage will be based on that appraisal, and therefore the second mortgage is high because the purchaser usually has not the equity to meet the difference.

MR. GRAHAM: We do not recommend any broadening in this connection of the basic test that you can only deduct interest on money borrowed for the purpose of earning income, and that would open the whole can of worms to which the Chairman has referred.

We are confining ourselves exclusively to the situation where for reasons beyond his control, normal maretability, and as you suggest, the inflated prices of real estate, he has no choice but must accept a mortgage on the property he sells. He thereby has investment income which he reports and then he turns around and buys a house and has to put a mortgage on that.

We suggest this is unfair, and is something which should be rectified, and it should only be against investment income.

COMMISSIONER GRANT: I think I would make the observation that sometimes he is very happy to accept a second mortgage as a form of investment. Of course if he has to go out and buy another property, I can see where your point comes in, but if you could restrict it to this buy and sell, you might have a pretty valid case.

On the other hand, it would be difficult, would it not, to restrict it to the cases where a person has been forced to take a mortgage on a property which he would not have had to take, or give a mortgage which

he would not have to give, had he got the money out of the first transaction? It would be very difficult I would think in point of law to restrict this type of tax relief to situations such as that, would it not?

MR. GRAHAM: I do not think it need be so restricted. If a man has $10,000.00 in bonds and he decides he wishes to keep that money in that form of investment, and then he puts a $10,000.00 mortgage on his home, there seems to be no logic or justification for saying he has to pay tax on the coupons from the bonds and that he cannot deduct the interest that he pays on the mortgage.

If we forget about mortgages for the moment, and he borrows money from the bank in order to purchase an investment, he can deduct bank interest in that case and offset it against income he receives from the investment. These should be on all fours.

COMMISSIONER GRANT: What about the person who has no mortgage on a property, and he is not contemplating the sale of that property, but he says "I think I will put a mortgage on my house and invest it in equities because I think I have a good chance to make a capital appreciation", so he does. He puts a mortgage on the house and he raises his money in that manner. Would you say that it would be the same there?

MR. GRAHAM: Yes, exactly.

MR. GIBSON: Exactly the illustrations that Mr. Graham has given: often a taxpayer in that position, if he seeks advice, will be advised instead of retaining his $10,000.00 in bonds and giving a second mortgage on

the purchase of his house, on which he will have interest that will be non-deductible, normally I think the advice would be that he first of all dispose of his bonds, use the proceeds to apply against the purchase of the house, and later raise a mortgage on the house in order to buy back the bonds.

This makes our system difficult to understand to a great many of our taxpayers. If I understand the law correctly, if the procedure were carried out in that way, the individual would say he borrowed money on the security of his house for the purpose of buying bonds, and it would quite likely be accepted.

MR. GRAHAM: Another variant, of course, is to pledge the bonds with the bank, borrow money from the bank, and thereby avoid a mortgage, in which event he can charge off the money he pays because he has borrowed money to hold the bonds.

It seems in our view to be an inconsistency and one that has very broad application and affects the average citizen from one end of the country to the other in the buying and selling of his home.

MR. TAYLOR: In recent years in some of the more sophisticated areas of investment, in recent years this has become a point of contention. Almost every time we have had occasion to move a man from one area to another, he has run into exactly this problem, and he uses it usually as an argument why we should pay him an increased increment of salary over and above what we would normally pay just because of the unfairness and inequity that he sees in this mortgage situation.

THE CHAIRMAN: By "we" you mean your company?

MR. TAYLOR: Yes, and as Mr. Gibson points out, this tends to create an image of unfairness which I do not think is a good thing to create among citizens. They become conscious of these things only when they hit them, and he bases his opinion on the system on how it affects him.

COMMISSIONER GRANT: I noticed in this morning's paper that a company is being formed. The Bill has passed the Senate and is now before the Commons. It is backed by the Bank of Nova Scotia, the Aluminum Company of Canada and Greenshields. The object of it is to get into the secondary mortgage market; into the conventional mortgage field. There is an insurance company involved where the risk is insured as it is under the National Housing Act to the extent that they will lend on a much higher percentage.

It probably goes as high as the National Housing Act is giving.

MR. GRAHAM: There was a full-page advertisement in the Toronto Press yesterday of a similar relationship developed by the Canadian Imperial Bank of Commerce.

COMMISSIONER GRANT: I read that.

MR. GRAHAM: It is roughly similar.

COMMISSIONER GRANT: I do not think there was any distinction under the Commerce plan on the percentages that they would take. I think they are just entering conventional mortgages the same as it is now being served by mortgage loan companies.

MR. GRAHAM: This is a somewhat new departure.

COMMISSIONER GRANT: Yes, quite a new departure. It is really to give the same service to the conventional mortgage field, as far as the amount of the mortgage, I think as is now obtainable through the National Housing Act.

THE CHAIRMAN: Can you gentlemen return this afternoon? I am sorry we have not got through this morning. I think we still have an hour left on this, or perhaps an hour and a half. We will stand over until 2:15.

---Noon Adjournment

---On Resuming at 2:15 P.M.

THE CHAIRMAN: Are you ready? Mr. Gibson, we move to Page 21 I think. Discount on Borrowed Money. In that section you make the suggestion some discount deduction should be permitted. This I have heard suggested before. I know that over the years many times people have thought that the law should be more generous with regard to this, but I think it is being pointed out that if it should be permitted as a deduction, it seems only fair to bring the other side over to taxable income. This does not do that, does it?

MR. GIBSON: No, it does not, and we have suggested that limitation -- I think this is not a novel recommendation. We recognize the difficulty or probable impractical nature of suggesting that this could be taxed in the hands of the recipients; it is hard to

identify who the proper person to tax should be.

On the other hand, we have attempted to suggest a limitation on the amount of discount that would be accepted for collection in a way that would permit sufficient flexibility for corporations to establish their selling price to the public at the last minute. In other words, this suggestion would at least permit the borrower to adjust to the market prices at a late date, and at the time of issue without suffering a loss from discount.

In other words, the amount of discount permitted, if our suggestion were adopted, would not be very substantial, but would permit some flexibility to the borrower in establishing the issue price.

THE CHAIRMAN: Would it be worthwhile to the borrowers to impose this on the administration of the law?

MR. GIBSON: It is our feeling that this suggestion we have made would not impose any substantial administrative burden. We do not feel that the amount itself or the calculation itself would be difficult to make.

COMMISSIONER PERRY: How would it work out in the normal course?

MR. GIBSON: The specific suggestion we have made is that the formula be used as is used in section 7 (2) which would permit a variation in the issue price from the par value equal to or in an amount sufficient to permit only one-third variation between the yield and coupon rate. In other words, if the coupon rate were

6 per cent, the yield could vary only to the extent of two points.

THE CHAIRMAN: Are there any other questions?

COMMISSIONER WALLS: On this last point you have raised about inequity of a retiring employee who is taxed on amounts received from a pension plan that was in effect at the time when he was not allowed deduction for tax purposes when paying into it. I do not know how you could correct that situation now. It would seem to me that administratively it would be rather difficult to be able to identify pensions now being received that fall within that category, would it not?

MR. GIBSON: On the recovery of contributions that were disallowed in the past, I think our feeling was if the responsibility were moved to the taxpayer to establish satisfactory evidence that he had been in fact disallowed a portion of his benefit, this responsibility of the taxpayer could be discharged if they were aware of the possibility and were at any stage disallowed a deduction for part of the contribution they themselves had made. They would obviously keep a careful record of that fact.

In other words, if the taxpayer were given a right to a deduction should he be able to establish the facts of the case --

COMMISSIONER WALLS: Is that in effect not making tax changes retroactive, and over the whole tax structure would not be feasible.

THE CHAIRMAN: Would you seek to correct an

inequity of tax?

COMMISSIONER WALLS: That is right.

THE CHAIRMAN: I am not a bit sure there is an inequity here at all. It seems to me this is income, and as such, should be taxed. The inequity, if there is one, is if he is not permitted a deduction of premium.

MR. GIBSON: I presume it could be looked at either way; that he has made a contribution on which he has had no tax relief, and is now receiving that amount back and is taxed on it, so that it could be looked at as recovery of his own money for which he had no tax relief.

I think this is the approach that the average person receiving recovery payments of this sort take. It is clear enough there must be some limitation on the right of an immediate deduction in respect to contributions, and the administrative problem is the only reason why some relief is not made in respect of the recovery of these amounts.

THE CHAIRMAN: Does this happen very often?

MR. GIBSON: Not in my experience, but it has been raised quite frequently with the Board, and I presume from that it happens more often than I would have thought.

MR. GRAHAM: If I may speak, Mr. Chairman, this is a question perhaps of repairing a deficiency in the handling of old pension arrangements. There were old pension arrangements which involved the purchase of individual contracts of insurance where, for example, the problem does not exist and only the interest element

is taxed.

On the other hand, if the payments went into a "pension plan", and come out and are not clearly segregated, and even sometimes where they are clearly segregated from benefits derived from contributions which were deductible, then the entire receipt is taxable.

Certainly if one were sufficiently sophisticated 20 or more years ago when these plans were established, one could have avoided the problem, but there are a number of plans where all of the receipt is now taxed even though there was no relief secured on payment in. It is to that category that this reference refers. I do not think they are too numerous, but there certainly are cases where, due to inadequacy of advice in establishment of these plans, people to-day are having to pay income tax with respect to amounts which in truth are a return of capital.

MR. GIBSON: This also arises in cases of plans that for one reason or another fail to qualify as a registered pension plan. The prohibition on the reduction of any capital element in respect to an annuity applies generally to any return or any recovery out of a pension plan whether it is registered or not, so that in some cases a person may be a contributor towards a plan that qualifies as a pension plan, but not a registered one, and he would be taxed on the entire recovery he received.

COMMISSIONER WALLS: I am rather surprised we have never had this problem put before us before?

THE CHAIRMAN: I am not sure that one should

seek to correct the matter of non-registered plans. Surely that is the purpose of registration, is it not, to see that the plan conforms to prescription, and if not, impose a penalty.

MR. GRAHAM: With respect, Mr. Chairman, surely the criteria imposed are in order to secure tax relief on payment in you have to comply with certain prerequisites. I think it would be erroneous to suggest that registration or the lack of it imposes a penalty on payment out. I think it is on the deductability from income at the time of payment in.

MR. GIBSON: There should not be really a penalty at all for failure to register a plan one would think, but a plan that failed to register should be accorded much the same treatment as an individual's contribution under an ordinary annuity. In other words, it has none of the benefits of tax preferment that are commonly associated with registered plans.

MR. GRAHAM: I think, with respect, the problem here is lack of effete advice to a number of people who have found themselves in this position, because I do think it is possible to avoid this result if one is well advised at the time the plan is established.

There are hundreds of people who are caught and are really paying income tax on the return of their own capital.

MR. GIBSON: It is a fairly common problem for individuals who are resident in Canada and are still employees of an American corporation that has a pension plan of its own, where the employee is making contributions

to the plan, but the plan, being the American plan, is not registered in Canada and may not be registerable under our laws.

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COMMISSIONER WALLS: Does it not apply to firms who wanted to supply or assist in supplying a pension for one individual on the staff without making the plan available to the whole staff and therefore it was not acceptable at one time as tax exempt or tax provided pension plan.

MR. GRAHAM: If the benefits were provided entirely by the employer I think it altogether reasonable the benefit should be classed as income in the hands of the recipient. If on the other hand it is provided in whole or in part by the employee, if it is handled through the purchase of an individual annuity contract, for instance, he would only pay on the interest, basically on the interest.

There are other cases where they were not handled so clearly one way or the other and where a man is being taxed on the return of his own capital.

COMMISSIONER GRANT: The nice question arises whether that payment by the employer to the employee is deductible as a wage or a salary or is it an ex-gratia payment.

MR. GRAHAM: The professional observation I make will be worth what it is paid for. It has always been my feeling as long as there was a divesting condition there was no responsibility to report it as income on the part of the employee nor was it deductible on the part of the employer. A payment post-retirement if reasonable in amount was deductible on the part of the employer and equally was taxable in the hands of the employee.

COMMISSIONER GRANT: Depending on the relationship that existed between the employee and the employer.

MR. GRAHAM: The word "reasonable" encompassed many things.

COMMISSIONER GRANT: I am thinking, to be definite on this, of a payment to a widow of an employee where there was no provision for a pension. In such a case I know it might very well be regarded as an ex-gratia payment and not permitted as an expense.

MR. GRAHAM: With respect, my experience in my practice is that the department will regard as reasonable a payment following retirement to an employee who has had a full measure of service, let us say not less than 20 to 25 years of service and they regard up to 70 per cent as being reasonable and to the widow of such employee a payment of up to one-half of that amount as not being unreasonable and being deductible.

I would not want to say what the statutory authority is. I refer only to the departmental practice.

THE CHAIRMAN: They have an English case which supports them in this.

MR. GIBSON: It is desirable this be so wherever adequate formal obligations have not been entered into. This is an obligation most employers regard as a fairly serious one even though it may not be a legal obligation.

COMMISSIONER GRANT: I don't want to labour the point but there could be a distinction between a payment to a widow of an employee who had not reached

retirement age and there is where they might regard that as purely ex-gratia.

MR. GRAHAM: That is quite possible. Again if it is "reasonable" I think the departmental practice, certainly in the local taxation office in Toronto, is to permit it as a deduction.

COMMISSIONER PERRY: There is one point I have. You don't have many taxpayers not contributing more than the allowable tax deduction on the pension plans, do you?

MR. GRAHAM: I have run into a number of cases, Mr. Perry. This goes to the question how to establish it. If they are contributing more my advice to the client is always to segregate the excess contribution to insure that tax on receipt will be applied to the appropriate part of the receipt.

If you do have a plan that requires "X" per cent of compensation to be paid in even on an amount in excess of the permitted maximum under the Income Tax Act then I think you are caught on the very thing that is referred to in this submission.

COMMISSIONER PERRY: This used to be stated as a common cause of double taxation. I must say we haven't heard about it yet before this Commission.

MR. GIBSON: I think it is uncommon. The tax penalty is not sufficient to deter an employee from making additional contributions. I have only one case.

MR. GRAHAM: I must say it is a wasting situation. I think it arose more when the deductible maximums were $300.00, $600.00, $900.00.

THE CHAIRMAN: Your next point is Cost of Income Tax Appeals. I see you recommend two things: "In cases where the Minister initiates an appeal to the Exchequer Court or to the Supreme Court, he should be required to pay the taxed costs of the taxpayer."

Your other recommendation is: "Legal and other costs of income tax appeals should be allowed as a deduction in computing income to the extent they are reasonable."

I have heard the first of those before. I can see the reason for it. The second I find more difficulty with it because it does not strike me that such costs are always incurred in order to earn income or in order to protect one's income and I would think the costs must meet one of the two tests to be permitted.

I would not like to extend beyond that or it would mean one was permitting this deduction for other purposes than to measure income. Perhaps that is what you intend, I don't know.

MR. GRAHAM: What we have in mind with the first, and it is implicit although perhaps not quite expressed, that it applies only to Appeals from the decision of the Tax Appeal Board. If the Minister initiates an appeal from the decision of the Tax Appeal Board then in any event, regardless of the result, he should be required to pay the taxed cost of the taxpayer.

THE CHAIRMAN: That is not so stated.

MR. GRAHAM: I think by implication. He can only initiate an appeal to the Exchequer Court or the Supreme Court where the decision of the Tax Appeal

Board is in favour of the taxpayer. We did not spell it out in sufficient detail.

THE CHAIRMAN: I didn't understand it. I thought he could initiate an appeal to the Exchequer Court without going through the first Court. That I take it is not so.

MR. GRAHAM: In theory I believe it is still so. In practice I believe they all go to the Tax Appeal Board. That is why I thought I should underline that.

MR. GIBSON: The Minister is not permitted to initiate an appeal directly to the Exchequer Court. Only the taxpayer can initiate an appeal.

THE CHAIRMAN: That is something I didn't know.

MR. GRAHAM: The second point, Mr. Chairman and Commissioners, is an extremely difficult area. We have no sympathy for the person who lodges a frivolous appeal and at the same time we have a great deal of sympathy for the person who lodges a serious appeal on a bona fide point be they successful or unsuccessful.

It seems unfair they should not be able to deduct the monies necessarily expended and that is, of course, what is implied in the last words "to the extent they are reasonable".

We first wish to acknowledge to the Board that this is not an easy area because there are always frivolous appeals by taxpayers for no good reason whatsoever. They just wish to have a day in Court but there are many cases where in our view it is unreasonable to deny at least deductibility of the monies nec-

essarily expended in prosecuting an appeal.

MR. GIBSON: We feel that taxpayers, particularly those who carry on a business, have an obligation that arises in connection with their business to compute their income and report on it and pay tax on it, and this is not always an easy tax particularly where the law cannot be and is not entirely free from any doubt and I think so far it has been held that the cost of settling disputes as to tax liability are not laid down to earned income. Perhaps they are to protect income that is earned and therefore not deductible. This does not seem a reasonable result.

THE CHAIRMAN: I suppose you can say dealing with income tax that almost every case is to prove or protect one's income. Gift tax also comes in there. Do you think it should be taken as a deduction?

MR. GIBSON: I don't think we had that in mind. In fact our recommendation is limited to income tax. I am perfectly sure the point had not crossed our minds.

THE CHAIRMAN: I was trying to search for something in the ambit about which you are speaking not concerned with income. Is there anything in the area in the income tax law not concerned with income?

MR. CRYSLER: Supposing a taxpayer were to venture into a transaction well within the normal activities of his trade and he lost money on it he would not be denied his expenses, would he?

THE CHAIRMAN: I don't think he would be under the law as it now stands.

MR. CRYSLER: We are proposing the principle might be carried into the launching on unreasonable grounds of an income tax appeal.

THE CHAIRMAN: I can understand the simple proposition. I am trying to see if you have not made it too broad. I am testing it to see if you have not taken a simple proposition to an area where I don't think it belongs. I cannot see much the matter with the argument you put forward. If it pertains it should be deductible. The fact it is concerned with the law does not make it less deductible. I am not sure if you just tie it on legal costs and don't have regard to the usual tests of deductibility, which is to earned income or protect, you have not made it too broad.

MR. GIBSON: I think there must be individual cases where assessment of the thing would lead one to believe it had been made too broad. I can visualize cases where the taxpayer defends himself against a tax certainly intended to fall on him and to allow him a deduction for the cost of objecting to that seems to be a bit thick.

I am inclined to think of those as the exceptions that should be accepted in favour of the general principle.

COMMISSIONER GRANT: Mr. Graham, on the change the brief has suggested in paragraph 1, I have been wondering as to what reaction this might have in your mind. If that change took place it would be changing, I would venture to suggest, for the first time the jurisprudence as it now stands and which is summed up in the

words that the costs follow the event, which is usually the case unless there is some particular reason for the facts to determine otherwise. This would breach or abrogate that principle. I wonder if that affects you in any way as a lawyer?

MR. GRAHAM: It is true to say that as between private litigants it is a well-established principle that costs normally follow the event but I suggest where you have on the one side a very large department of the Government and on the other side a taxpayer and the taxpayer's position is sufficiently sound to have been maintained by the first Court and the fiscus presumably for its own reasons of public policy desires to have that decision wiped from the books the individual taxpayer who may be the guinea pig should not have to pay for that privilege.

It may be something which has a far, far wider implication and the Department may insist on going right through to the Supreme Court in order to clarify a point of tax law which is way beyond the financial stake or interest of the individual taxpayer. Therefore in that case I feel that does not offend me in any way.

The cost of the taxpayer should be paid just as they are quite frequently on occasions in criminal appeals where the same type of situation sometimes arises.

THE CHAIRMAN: The merits of the case did not enter into it.

MR. GRAHAM: Not to my mind if you have passed the Tax Appeal Board and it has given a decision

favourable to the taxpayer.

THE CHAIRMAN: You mean these appeals are initiated by the Minister in order to have a base for taxation in the future and if they want the benefit of that decision they should pay for it.

MR. GRAHAM: Exactly. There is no reason why one litigant should pay for the privilege of establishing a law unfavourable to all other people in his same position.

THE CHAIRMAN: We will move on to Ministerial Discretion. I notice you have always opposed Ministerial Discretion and I gather you still do.

MR. GRAHAM: That expresses the position of the Board very succinctly. We refuse to believe it is beyond the competence of legislative draftsmen to establish a principle sufficiently clearly for the Courts to understand.

THE CHAIRMAN: Do you believe when Ministerial Discretion is introduced into the Act it represents bankruptcy of ideas to accomplish by direct means a phrase or an action which would be written into the Act completely. It is only the failure of wits.

MR. GRAHAM: The language is yours, Mr. Chairman. We feel there is inadequacy of research and drafting talent and decision to have to resort to Ministerial Discretion.

THE CHAIRMAN: Most countries do in some respects.

MR. GRAHAM: So? With respect!

MR. GIBSON: Most countries face the same

problem of difficulty in expressing intent in language that will not make it possible for people to overcome the intent.

THE CHAIRMAN: We usually term things on whether or not there is a business purpose, or some such phrase, and one gets to those things. I suppose the draftsmen feel they cannot set down especially good rules to guide a Court in forming a judgment.

MR. GRAHAM: If I may say, Mr. Chairman, acquainted as I am with some legislative draftsmen, I question if it is inadequacy of the draftsmen. I think it is muddled thinking on the part of the administration that seek to catch something and they are not quite sure what they wish to have. There are some undisclosed holes in the armoury to which resort can be had. We have successfully gotten along without Ministerial discretion except in a very narrow ambit for some fourteen years. We are opposed to the reintroduction of Ministerial discussion into administration of the taxing statute.

MR. GIBSON: We are inclined to feel the impediment this sort of legislation places on the business community and the taxpayers generally is likely to be understated or at least not generally recognized where there is something of this sort. 138(a) is a very good illustration and is written in very broad terms and can be used, depending on the interpretation placed on the purpose of the thing by administration in the circumstances for which many feel it was not intended in the first place and is probably never going to be used.

Nevertheless this means that taxpayers in con-

sidering a proposed transaction must either obtain in advance a ruling that it will not be used, which will be very cumbersome process, or refrain from taking any action whatsoever that could give rise to a liability under those provisions. I think it is a very serious impediment that could cause a great deal of harm.

THE CHAIRMAN: The impediment is uncertainty. There are laws of this sort which are rendered less offensive to the business community by granting prior rulings. Would that solve this one?

MR. GIBSON: It would be essential, I think, if Ministerial discretion is widely used to solve the problems faced. I don't think it is a satisfactory sort of device in view of the cumbersome nature of application for rulings on relatively small items. Often on a great many cases it would be necessary to obtain them in individual circumstances and not rely on any statement of general principles that could be applied in a number of cases.

THE CHAIRMAN: The U.K. makes provision which permitted rulings under circumstances something like 138(a). They are not identical but in this general area on inquiry within and without the Government it seems to have worked satisfactorily.

MR. GIBSON: I think it must be essential if there is to be a provision of this sort. It is not as satisfactory as having a general statement of law that can be interpreted within reason by the Courts. It has been our feeling if the Minister in his wisdom can decide on individual cases how to exercise discretion

in some reasonable way he must have established some principles in his mind and it should be capable of expression, capable of interpretation.

THE CHAIRMAN: Whatever he has in his mind should be capable of being written down and passed to somebody else.

MR. GIBSON: We all suspect that the rules will be made up as they go along and this we don't feel is a satisfactory framework for business to be carried on.

MR. GRAHAM: If I may have a comment I would far rather, and I think the Board would far rather, rely on a body of jurisprudence built up in the Courts through the normal process of adducing evidence, examination and cross-examination and so on, than determining from time to time.

There is the old legal expression "the length of the Minister's foot" -- how does the Minister or the Deputy feel in respect to this case -- this is no basis for determining liability for tax in our view.

THE CHAIRMAN: It sounds like the discussions we had in 1947 and 1948.

MR. GIBSON: I have one further comment. Reference was made, I think, to discretion in the hands of the administration which in the context I think differs substantially from this form of discretion we are speaking of now. It is the kind of discretion that is placed in the hands of the administration through use of words like "reasonable", "fair amount", "fair value", which are of quite wide discretionary

authority and administration and nevertheless always backed up by, from the taxpayer's point of view, the right to appeal to the courts.

MR. GRAHAM: If I may add one further word perhaps by way of illustration. Mr. Gibson referred to the inhibiting effect of section 138(a). I think we observed the inhibiting effect in recent proposals made some months ago to the Congress of the United States.

As long as they remain on the order paper and not enacted they are inhibiting all sorts of ventures which, if the legislation was enacted, at least people would know where they could go and couldn't go. This is the very type of thing we fear. You don't know where you can go or where you cannot go.

THE CHAIRMAN: We will move on to Sales Tax. You previously indicated on Page 12 if there is not enough revenue or if we, in order to carry out our instructions felt it was necessary to turn over taxes to make up for the revenue lost through reduced rates of taxes on corporations and individuals,that there might be more revenue derived from increased sales tax on goods consumed in Canada than on material and equipment.

Are you thinking of raising the rates, widening the base excepting the part of the base that applies to materials and equipment or both?

MR. GIBSON: The Board did not entirely agree on the method that might be chosen. First of all we had some debate as to whether we would recommend, as a Board, the shifting in the level at which sales

tax would be levied. Many members of the Board, perhaps the majority, favoured a move to the retail level for sales tax for a number of reasons. There was by no means unanimity on this point, as one would expect in an organization with many varied interests as the Board. For this reason we made no recommendation on the point. Our concern here was we felt greater reliance in raising revenue should be placed on this form of taxation rather than trying to direct attention -- whether it be broadening of the base or increase of rates -- I think our suggestion implies increase in rates because any substantial broadening of the base would almost inevitably run into the very thing we are asking not to do, that is broadening of the base to include services and so on that rather largely enter into the cost of production of the goods manufactured.

THE CHAIRMAN: I would be interested in knowing whether in your discussions manufacturing sales tax had any friends.

MR. GIBSON: Yes, I think the majority, if I am not incorrect, were in favour of the retail level for a number of reasons but that was by no means universal.

MR. GRAHAM: We have a number of retailers who are members of the Board!

THE CHAIRMAN: It is a wonder you didn't compromise on wholesalers. Probably there are few of those!

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COMMISSIONER WALLS: It would seem to me on Page 12 you are being a little inconsistent. You want sales tax to increase the revenue lost by your recommendations on both corporation and personal income tax. Then you want to exempt machinery of production from the sales tax.

Surely the sales tax on machinery of production would be a very infinitisimal percent of the selling price of any product. Have you ever stopped to figure out just what effect it would have on the selling price of a product either in Canada or for export?

MR. GIBSON: We have seen illustrations of situations, particularly taxpayers, where the amount of sales tax in respect of machinery and equipment even at the present rate of 4 per cent will amount to a very considerable sum and may very well affect the profitability or otherwise of the enterprise. It depends really very much on the relationship of equipment costs as compared to other costs of production, of course, but in some types of business where equipment is used up very rapidly and there is a very heavy capital equipment content in the cost of production, it can represent a very significant amount.

COMMISSIONER WALLS: Let us just see. I will put some figures, and you can check me if you think they are wrong. First of all, we have to make some assumptions. Let us assume that the life of the machinery in question is ten years. Let us go forward two years to the time when the 11 per cent sales tax

is in effect. Not 4 per cent. The 11 per cent then would work down at 1.1 per cent per year, would it not, on the ten-year life of the machines? Is that right?

Now, your capital cost allowance on this machine let us assume also is 10 per cent so that would cut off .1 per cent and you would be left with 1 per cent as increase created by the 11 per cent tax.

MR. GIBSON: I am lost I am afraid.

THE CHAIRMAN: I think we got to the 1.1 per cent per year on the machinery quite happily.

COMMISSIONER WALLS: Let us break away from that. If I buy a machine for $100.00, and I pay 11 per cent sales tax, that is $111.00. Then do I not take my depreciation on the $111.00?

MR. GIBSON: Yes.

COMMISSIONER WALLS: Therefore I am taking depreciation off the 1.1 per cent, which leaves me with 1 per cent. It actually does not make much difference whether we use 1 per cent or 1.1 per cent.

MR. GIBSON: No, no. That is right.

COMMISSIONER WALLS: Now I think it would be safe to assume that a very high average of the amount that machinery has to the cost of a product would be about 20 per cent, would it not?

MR. GIBSON: I think it varies tremendously as between different types of business.

COMMISSIONER WALLS: That is a high average?

MR. GIBSON: I think that might be a good high average.

COMMISSIONER WALLS: That is all we can do,

take a high average.

MR. GIBSON: I should think we ought to protect ourselves against putting out business industries that have a much higher than average --

THE CHAIRMAN: How high can you get? 40 per cent?

MR. GIBSON: Yes, it might be as high as that.

COMMISSIONER WALLS: We will take it both ways. If it was 20 per cent, then you would be left with one-fifth of one per cent as the amount that would be added to the cost of the product, and if it was double that, it would be two-fifths of the one per cent.

MR. GIBSON: I would question that. It seems to me if 40 per cent of your sales value is going in machinery cost, and you increase the machinery cost by 11 per cent, it would be something in the order of 4 per cent.

COMMISSIONER WALLS: It would be .4 per cent, if you are taking the life of the machine over 10 years.

COMMISSIONER PERRY: You are assuming it is amortized in the one year.

MR. GIBSON: No, I am merely assuming we are talking about an industry that starts from to-day, and you add 11 per cent to the cost of its equipment, and each depreciation claim over the life of the equipment, the equipment cost is going to be 11 per cent higher than it would have been.

COMMISSIONER WALLS: But you would spread that cost against the product you produce over the next

ten years.

MR. GIBSON: That is true.

COMMISSIONER WALLS: That is the difference between our figures, and that is why it brings it down to .4 per cent instead of 4 per cent.

MR. GIBSON: I must reserve judgment at least until I have had a chance to work it out.

THE CHAIRMAN: If you raise your equipment cost by 11 per cent, you are raising by 11 per cent the equipment proportion of the costs of your goods, and you need have no regard for time whatsoever. The time factor does not come into it. Your equipment is costing you 11 per cent more than it would otherwise cost you, and if your equipment costs are 40 per cent of your goods, it is going to be 44 per cent of your goods instead of 40 per cent. It has nothing to do with whether it is spread over 10 years or 5 years; is that not right?

COMMISSIONER WALLS: I do not think you are right. I think you have to take into consideration the 10 years. What you are saying would be quite justified if you were going to charge the whole cost of the machinery in the first year against the cost of the product.

MR. GRAHAM: If I might get into this, I think, Mr. Walls, you would agree at the end of 5 years even with capital cost, the machinery is still costing you, standing you 11 per cent more than it would have stood you had you not paid sales tax on it.

COMMISSIONER WALLS: Not if you have depreciated it in the first five years.

MR. GRAHAM: I was taking your example of the 10-year period.

COMMISSIONER WALLS: But then I depreciated it.

MR. GRAHAM: But it is still standing on your books at 11 per cent more than it would stand on your books had there been no sales tax.

MR. GIBSON: In effect if we take a piece of machinery that will last ten years, and we intend to amortize it in equal amounts over a 10-year period, the assumption we have made is that, say, 20 per cent of the selling value of the product was represented by machinery cost; that would mean one-tenth in the first year represented 20 per cent of the selling value of the product. If that machine in total cost 11 per cent more than before, each of the one-tenth segments goes up by 11 per cent.

COMMISSIONER WALLS: Then it would be one-tenth of the 11 per cent.

MR. GIBSON: In the first year, but that represents 4 per cent of the charge against the product for that year, which I think would represent about 4 per cent of the selling price in our example.

MR. GRAHAM: The essence of the Board's recommendation was that any equipment used to manufacture goods, be it for export or for domestic purposes, sales tax should not enter into that, firstly, to make Canadian products as competitive as possible in

the export field, and secondly, to enable them to compete on an even basis with imported goods that do not bear this tax in the same way.

That was really the essence. The arithmetic can get extraordinarily complicated, but we were concerned about making Canadian manufactures as competitive as possible.

COMMISSIONER WALLS: Let us look at it in the two ways you have mentioned. The second way is that you wanted to be competitive with imports. You fully covered that in your section here dealing with sales 2 tax. Of course that would be cured if the sales tax were moved forward.

MR. GIBSON: Yes.

COMMISSIONER WALLS: That problem would disappear?

MR. GIBSON: Yes.

COMMISSIONER WALLS: Insofar as exports are concerned, I do not know that using other countries is much of an example, anyway, but the fact is when research has been carried out, three European countries who are large exporters, have charged the tax on machinery of production, and it apparently has not affected their position in world markets.

I am just wondering when everybody is concentrating on this and wanting to take a load off here and put it all on sales tax, if we are justified then if we start requesting further exemptions in sales tax.

MR. GRAHAM: I think it is difficult to get a true comparison with European countries, having

regard to the other elements that go into the cost of Canadian production, such as wages and other programmes which are imposed on the Canadian manufacturer which, percentagewise, may well be larger than those in European countries. Certainly our wage levels are higher.

COMMISSIONER PERRY: The economists will say you really cannot impose indirect taxes in such a way that you do not increase your cost of production.

MR. GIBSON: I think obviously this must be so in the long run.

COMMISSIONER PERRY: Even if such an indirect way that all it affects is the cost of living index, it will affect your labour costs.

MR. GIBSON: This may have that effect, but if the country takes on responsibilities that cost too much for them in effect then labour costs can't grow. This type of discussion gets a little beyond the competence of people who, like ourselves, are not experienced in the arts of economics.

COMMISSIONER PERRY: I think it is simply that taxes normally are cost, and for the most part commodity taxes are more directly a cost than income taxes. To the extent that if you switch from one form to the other, you are bound to have some effect on your cost level.

The argument is made that if you do not make compensating changes, if your prices do not go down to compensate your reduction in corporation tax to the extent they go up because of the other taxes, then you are worse off than you were before. I am just throwing

a big wrench into this.

MR. GIBSON: This may be so. It would appear to us as easy to see in comparison, or at least when considering the competitive position, for example, of a Canadian purchaser of goods in competition with an importer; but if the same amount of revenue were raised from the sale of goods imported and the sale of goods manufactured in Canada, that this then left the two on an equal footing.

If the Canadian manufacturer bought some element of tax that was not imposed on the manufacturer of the imported goods, this left an advantage to the importer.

COMMISSIONER PERRY: It could apparently be a disadvantage under some conditions.

COMMISSIONER WALLS: I note you are going to go one step further and recommend exemption on transportation. You now also want it on transportation. I presume you mean removal of sales tax on trucks and other means of transportation?

MR. GIBSON: We felt this was a very broad recommendatin and one that should be given a good deal more study than we have given it. It was suggested to us in the Board that transportation has been such a vital factor in the growth of this country, and distances are one of the major impediments to the growth of our industry, that consideration should be given to giving some inducement or some assistance to the transportation industry towards the task of keeping the cost of transp-portation as low as possible, and this might be done

through the medium of giving exemptions to forms of equipment.

THE CHAIRMAN: And then raising taxes elsewhere?

MR. GIBSON: Presumably, yes. Unfortunately.

COMMISSIONER WALLS: So we make this circle. I think it would be extremely difficult to give a tax exemption on trucks. You are specifying here the use of the truck, and if you give it on trucks, you would have to give it on all forms of transportation, and insofar as the percentage of tax on a truck, considering the mileage that it covers, I do not think it would make it any material amount less on transportation costs. Do you think so?

MR. GIBSON: I simply am not sure. This is an area we have not given enough study to in order to make a specific recommendation.

THE CHAIRMAN: Now, estate tax. You point out when the capital levy at death becomes confiscatory or requires the liquidation at sacrifice prices of a business venture, serious problems result.

We keep on seeking evidence of the damage which is caused by these capital levies and what evidence there may be as to the sale of businesses at sacrifice prices, if some have occurred. I do not think anybody has supported such a statement very well so far.

Do you know of any business that has been sold at a sacrifice in order to pay estate taxes?

MR. GRAHAM: In commenting on that, Mr. Chairman, I have appeared before the Commission before

with respect to representation on this particular statute.

THE CHAIRMAN: I think we have asked you this question before.

MR. GRAHAM: You have, sir, and it is extraordinarily difficult in all honesty to produce from trust companies, solicitors or others specific examples that they are prepared to vouch for and to have go forward.

I sincerely believe that this is not something which is merely an impression. Certainly the amount of time that is spent by taxpayers in endeavouring to so arrange their affairs as to ensure continuance of business and provision of funds would seem to indicate that the problem is real and does exist.

I can mention of my own personal experience of a few cases where businesses, because of lack of provision, had to be liquidated more quickly than would have been desirable from the standpoint of the ultimate realization by the estate.

Following my earlier appearance, I caused a circular to be sent to all the members of the Trust Company Association, and I must say I was extremely disappointed in the results. They all said, yes, yes, we know all about this, but we do not have any papers we can give you, which was not helpful from the standpoint of the Commission or of my undertaking to the Commission.

THE CHAIRMAN: I might say, Mr. Graham, we tried this out on the trust companies, and to the best of my recollection, they agreed to go back and re-

consider the matter and endeavour to search out some cases and to let us have some further information. I suspect we have not heard back from them yet. I think they have not had time.

COMMISSIONER PERRY: That is right, both domestic and foreign investors.

THE CHAIRMAN: Like you, I find it very difficult to come down on this thing in such a way that I really can get much support for this generally current opinion that one hears discussed everywhere. It is before us very frequently.

MR. GRAHAM: Of our recommendations, there is one that is related to this which I think is extremely important, and that is ability to settle tax over a period, and with proper security and proper rate of interest.

It is not everyone who is able to provide, through life insurance, for example, for sufficient liquid assets on death to settle tax within six months and thereby avoid penalties.

THE CHAIRMAN: If the amount is secured, it seems to me perfectly reasonable. There may be things that I have not thought of yet.

MR. GRAHAM: I see no reason against it, and that is the recommendation we made strongly, that there should be this opportunity to settle over a determined period.

As to the first part of this paragraph to which you were referring, again I endeavoured to get more examples. I can give you examples now. I can give

you one who left Canada at the end of August, and someone who left Canada last February, and in each case they moved to Nassau.

In the one case it was an 87 year old woman who has an estate substantially in excess of one million dollars. She has one child, who prevailed upon her -- it would be a very desirable thing for her to finish her days in Nassau, which she is doing, and the Canadian Exchequer is going to be the recipient of a substantially lesser contribution on her death than it would have been had she remained in Canada.

The other is a younger person who relies upon dividends and interest, investment income, and again a translation of locale to Nassau, and once again for the same reason, which is a reduction in the tax liability.

Those are two cases that I have had in my own practice this year. The first one is an extremely elderly lady, who I may say had never been outside Canada in her life, and her son presented the idea, and she backed the idea, and it is going to make a difference of several hundreds of thousands of dollars -- the payment of taxes is anathema to her, so she migrated to Nassau.

There are cases of this kind that are growing within the practice of each professional man who indulges in this type of practice.

THE CHAIRMAN: I am sure they are, and I am sure we are losing tax because of it. If we were to figure out, I suppose, what the point of maximum return is -

MR. GRAHAM: I can only say the taxes are inducing some people to migrate.

COMMISSIONER GRANT: In that particular case, she has divested herself of all interest in Canada, including her responsibility, securities; everything has been taken down to Nassau?

MR. GRAHAM: No, she has changed her domicile by selling her home and buying her home in Nassau, and a cemetery plot. She has no intention of ever returning to Canada. I think it is quite clear she will never return to Canada. All her securities remain in the custody of a Canadian Trust Company, as they have for some years.

I do not think that is the criteria in this case as to change of domicile, and the Estate Tax Act is based on domicile.

COMMISSIONER GRANT: I was just wondering if she will be successful in divesting herself of her domicile of origin, which you know it is a very difficult thing to shake clear of.

MR. GRAHAM: I would think she would be. There may be some dispute.

MR. GIBSON: In connection with the purpose of the tax, it has been our assumption, and we have stated that we do not regard tax as intended primarily for the purpose of raising revenue, but more as a social device for levying huge accumulations or curtailing excessive accumulations, and it is looked on in that way. The objective should not be necessarily to adjust the method and rates of tax in such a way as to maximize

revenue. Perhaps it could be put more closely for the purpose of eliminating what may be properly regarded in this day and age as excessive accumulation of wealth in individual hands. Our view really is that the rate structure is not appropriate in that at the present time.

THE CHAIRMAN: It was pointed out in something I read the other day that traditionally all succession duties of estates were the property of the Crown.

MR. GRAHAM: Leave us not return to the mediaeval days.

MR. KIRK: I know of one example, and I do not think there is any secret about it. As a matter of fact, I think the man involved might be willing to testify himself. He had one of the larger contracting companies in Toronto a few years ago. He was the sole proprietor, and he sold out to an American company, and the real reason, the sole reason, I understand was succession duties.

His duties took him in small aeroplanes to Northern Quebec and Western Canada, and he felt there was a fair chance he might be killed, and if so, the business may have to be liquidated in order to pay succession duties so he sold the whole thing out to an American contractor who is running the company now in Toronto. I think probably I could get him to state so himself.

THE CHAIRMAN: I think your story is a most reasonable one, and I do not think we have any reason to doubt it.

MR. KIRK: I just didn't know whether or not I cold make public his name, but I think he himself would be willing to testify to that.

THE CHAIRMAN: We would be glad to hear from him. It would be a concrete example, and it is pretty hard to take these things without examples.

The people who moved to Nassau have mixed motives quite obviously. Succession duty I would think would come into it, but also the Nassau climate would come into it.

MR. KIRK: This chap is 47 years old, and he is now working for Billy Graham, after building up a big company in Canada.

COMMISSIONER GRANT: He has got religion.

THE CHAIRMAN: Is there anything futher on the nature of the tax? If not, I shall move on to the significance of the tax to the Exchequer.

You recommend that the tax be applied only from $100,000.00 up. As I understand your recommendation, you do not recommend the abolition of tax completely there, and that is because you believe there is probably some social justice achieved by the tax which would not be achieved if it was not there.

MR. GRAHAM: I think it is our view, Mr. Chairman, that a tax on death is now accepted in Canada to such an extent that certainly the Board of Trade of Metropolitan Toronto is not advocating the abolition of such tax apart entirely from the complete lack of feasability from a political standpoint.

COMMISSIONER WALLS: We have had the suggestion

made there is only a total revenue of eighty million dollars in it, and it should all be turned over to the provinces to run their own succession duty, and the Federal Governments to get out of estate tax.

You take the attitude here that the Federal Government should definitely be in the estate tax alone and make agreements with the provincies for amounts that they will collect on their behalf? Is that right?

MR. GRAHAM: Yes, and the reason for that recommendation by the Board is primarily an administrative one, We feel that there is unnecessary expense involved in multiple jurisdictions levying taxes on different bases . Varying statutes make proper planning much more difficult, and it would therefore be very much in the public interest in all of Canada if there were a single statute.

We do not take any position as to whether any of the money should stick with the Receiver General of Canada or whether it should go to the respective Comptrollers of Revenue, Provincial Treasuries or what you will, but only from an administrative standpoint there should be a single base of tax because so many people have assets in varying provinces, and it does seem to be something which complicates unnecessarily the location of businesses, the responsibility of individuals, and the control of their investments. A single system would have so much to commend it, that we advocate that very strongly.

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MR. GIBSON: The method of tax is implied in the Estate Tax Act and is, I think, considerably better from the point of view of planning by taxpayers to take care of their responsibilities, predicting what the liability will be then as in the case of the Provincial Succession Duties that depend, among other things, which of the relatives will survive and so on.

For this reason it may be desirable and perhaps almost essential if uniformity is to be achieved on the Estate Tax type of tax.

THE CHAIRMAN: If you want to bring the exemptions up I find it difficult to understand the justification for bringing the top rate down to 30 per cent. It would seem to me that that is a pretty low tax on a very large estate by our standard as things now stand and it seems to me that there must be some relationship between Estate Taxes and Capital Gains Tax. I would have thought if there were no Estate taxes in Canada there would be a much stronger case for Capital Gains Tax. Does that not all add up to the result that we ought to have a fairly steep top rate of Capital Gains not a weak one.

MR. GRAHAM: You mean death tax?

THE CHAIRMAN: Estate Tax, I am sorry.

MR. GRAHAM: If I may make a comment, this was not discussed in our Committee. It might be said the ground rules have been changed within the last week with the proposals that came out of the Federal - Provincial Conference.

Speaking therefore only for myself as an

Ontario resident, Ontario has paid more, more has been exigible on the death of Ontario decedents than on decedents in other provinces. Part of the reason for the 30 per cent is that Ontario is still very much in the field. How this will inter-relate now if 75 per cent is to go back to the provinces I personally cannot comment. I would like to put a question mark beside the submission of 30 per cent from my own personal standpoint. I don't know if my associate would or would not. The ground rules have changed for us since we prepared this submission.

COMMISSIONER GRANT: Incidentally, the increase from 50 per cent to 75 per cent does not in your opinion lessen the chances of other provinces coming in if they think the traffic will bear the increased tax.

MR. GRAHAM: This, sir, is political crystal-balling and I cannot indulge in it with any degree of success.

COMMISSIONER GRANT: I was going to ask you about the fifth recommendation on Page 29. That is where the valuation shall take place within six months of the date of death, or at the date of death, but at the option of the taxpayer and that has been the recommendation that has been made to the Commission by several others.

In the event of what has occurred in the last two weeks, the death of President Kennedy and the effect which that had on the stock market, for instance if the estate fell into being within that period and the market was off 22 points it strikes me these things

do occur fairly frequently now. There are international events that change the market overnight, there are political events. I am wondering if it is entirely fair that the estate should be in a position of being able to say we want to take a certain date in that six months. Would you consider there should be an averaging?

MR. GRAHAM: Mr. Chairman and Mr. Grant, all of these bases of valuation are arbitrary unless one requires realization as to the value on the basis of what is realized. The speed of administration, the certainty of administration are matters of very great import. We don't recommend an alternative valuation date more than six months after the date of death.

If you have a longer period there would be a difficult onus laid on any fiduciary to determine whether or not he should sell or should not sell. I feel and the Board feels it is in the public interest and the interest of heirs that estates should be administered as expeditiously as possible.

Then you come to the determination of value and the traditional approach in this country has been the date of death. It is the Board's feeling that potentially this could cause great hardship. There may be factors present as of the date of death when it is still a going concern and where the influence of the proprietor is still very strong which would be removed very soon afterwards and a week or two weeks after the business may be worth less than at the date of death and therefore you get into some other arbitrary basis which imparts as much fairness and reasonableness as you can to avoid

a penalty against the estate. One could equally well say three months, six months, nine months, or twelve months. Our feeling is this is a reasonable straddle. It is either value at the date of death or six months hence or if you realize in the meantime the figure at which you realize. It is equally arbitrary to the present basis. We do feel in appropriate cases it could give appropriate relief to estates that might otherwise be penalized.

Obviously I would think one must acknowledge that there would be some decline in the revenue raised from the tax because any trustee is obviously going to elect the lower of the two. At the same time what is the purpose of this tax? You get back to the philosophical question: is it not better to take a realistic figure and value fairly and levy the tax on a fair basis than on a value ascertained as of the one day in the whole history when you cannot realize on the asset.

COMMISSIONER GRANT: The emphasis of my question was not on the term of the six month period but it was that the valuation within that period should be entirely at the option of the estate.

MR. GIBSON: May I clear up one point that might be troubling Mr. Grant? It is not our intention to recommend that the estate be entitled to choose any date within a six month period but merely to choose either the date of death or the date six months following the date unless the assets have in fact been disposed of in the meantime at which case whatever the realization value is would be taken.

COMMISSIONER GRANT: Let us refer to the example I took. We had a market that was off 20 points in one day. That could happen quite frequently. I dont think it is a fair method of appraising an estate.

COMMISSIONER PERRY: I was surprised people are willing to settle for this proposal. It is just as likely one day six months hence is going to be as abnormal as the date of death.

MR. GIBSON: That is the date the assets can be realized.

COMMISSIONER PERRY: It may be the day the world ends. You are taking a gamble between two arbitrary points. This seems to be a palliative rather than an effective cure. It means you are willing to gamble on one day six months later being a normal day.

THE CHAIRMAN: They might prefer one month.

MR. GRAHAM: The Board endeavoured to be realistic and tried to give some certainty to administration. I know of no jurisdiction that permits an averaging or gives you a whole series of alternative dates. Our purpose here was in the event there was a artificially inflated figure or price that could not be realized at the date of death to give relief in that case so the tax would in fact be levied on the amount that did in fact pass through the hands of the personal representatives.

MR.GIBSON: If this were adopted, if the six month after death date were chosen the estate would have the right to dispose of assets.

COMMISSIONER PERRY: Now you are getting at

something significant.

MR. GIBSON: This is contained in our recommendation. Any assets sold in the period would be automatically valued.

COMMISSIONER PERRY: You can see substance in that.

THE CHAIRMAN: Those assets sold in the interim period the realization would be added to the value of the remaining assets at the end of the six months, I would assume.

MR. GRAHAM: Or at the date of death.

THE CHAIRMAN: All right. Possibly there would have to be a rule governing that.

COMMISSIONER PERRY: I think this is another one that is not as simple as it appears. I understand the American provision is quite complicated.

MR. GRAHAM: As I visualize it you have an estate consisting of three assets. One of them is sold three months after death and that asset is valued at the amount realized.

MR. GIBSON: No matter what date one chooses.

MR. GRAHAM: The first asset you might choose to value at the date of death, the third asset six months later, and the one sold within the six months is inventoried at that amount.

COMMISSIONER GRANT: The date you determine what the valuation is going to be is the date you file the estate tax return. That is the date you make your comittment and you stand or fall on the valuation as of that date. If you have a feeling you are going to win

by waiting six months you will wait and not file a return until the end of the six months and at the eleventh hour you can make a return and say "Here they are." Any assets sold in the meantime are going to be inventoried and listed in the assets of the estate at the value they have brought.

MR. GRAHAM: That is correct. It would seem to me if the estate consists of assets subject to variation the personal representative would be almost afraid to wait six months in the proper discharge of his duties before filing his return.

COMMISSIONER GRANT: You are placing a great burden on the executor if this becomes law. It is quite a choice for him to make. He has no alternative to-day but he certainly would have an alternative if this went into operation and it would throw quite a burden on him to make that decision. He could be subject to praise or damnation.

MR. GRAHAM: Executors currently are.

THE CHAIRMAN: Anything else on this one?

MR. TAYLOR: Mr. Chairman, as I told you earlier I have an appointment with the U.S. Ambassador and I would like to get to it. I thank you for the opportunity of presenting our brief to you and for the very complete and interesting review you are in the process of making. I am sorry I cannot stay until the end of it but it is obvious, I think, that I am not contributing too much to the discussion.

THE CHAIRMAN: I don't think that is true. I would like you to know we appreciate very much all you

have done in your submission to us and we would like to thank you for the manner in which you have been able to back it up.

Thank you, Mr. Taylor, indeed. The rest of you would like to catch the five o'clock plane?

MR. GIBSON: If possible.

THE CHAIRMAN: I have one question under Gift Tax. Perhaps the others have some more.

MR. KIRK: I think we have an initial statement on the Gift Tax.

MR. GRAHAM: Mr. Chairman, there is a significance which I think will be apparent to you. The initial paragraph under the heading Gift Tax although it is true it is by no means wholly true. Gift Tax was in fact enacted prior to the imposition of the Estate Tax Act and there presumably were other reasons than the one recited there that activated the Government of the day to introduce it.

So far as Gift Tax we were in a bit of a quandry as we were unable to find out the amount of revenue raised by gift tax. The Board has the feeling that gift tax provides quite an insignificant amount of revenue. We may be dead wrong because there is no way of knowing.

COMMISSIONER PERRY: It used to be so up until about two years ago. I think three or four million dollars, as I recall.

MR. GRAHAM: It was our feeling if gift tax is to remain it can be only gifts more than three years prior to the date of death. Gifts within the

three years are caught under the Estate Tax Provision, speaking particularly and forgetting rates for the moment, if it is to remain the amount of tax free gift should be substantially altered. These rates were set twenty-eight years ago and four thousand dollars may have then been a significant amount. We suggest there has been many changes occurring in the last twenty-eight years.

THE CHAIRMAN: The critics of the U.K. inheritance tax point out the need for gift tax to pick up tax which is escaped by gifts and that is, I would think, the chief purpose of our tax. If that is the case surely there should be a closer relationship between the gift tax laws and the inheritance tax laws. Also while exemptions might be increased I would think the rate should be increased to bring it in line with the inheritance tax. Would that not follow?

MR. GRAHAM: I think that might well follow. One point could be made that gift tax is not shared in any way with the Provinces and yet gift tax is a deduction from the estate and thereby affects the amount of the estate that is subject to provincial succession duties. It is our feeling it is a tax which is a companion piece to the Estate Tax Act and as you say if it is to remain it should be integrated in some way. We are speaking to some extent in ignorance because the statistics are not available.

If the gift is within three years it is then caught for estate tax purposes and inter-vivos disposition. We are not happy with it the way it is at the present time.

MR. GIBSON: It may be questionable whether rates should be increased in order to act as a better companion piece to the Estate Tax. It would be shown to be true if more resorts had been made to the Gift Tax. As Mr. Graham pointed out he knows very few people who can be persuaded, even though it is in their best interest apparently, to incur the Gift Tax. I think it may be that the present rate structure represents a fair balance between the two.

MR. GRAHAM: Certainly a living taxpayer regards the Gift Tax as a capital levy, as in fact it is, and he is scared stiff of it. I find it almost impossible to persuade anyone to suffer the gift tax in order to implement some part of his estate plans. This just offends them, the whole idea of a capital slice taken off every gift they make.

THE CHAIRMAN: I have seen them take advantage of exemptions many times but usually they only make gifts up to the amount of exemptions whereas it could be highly advantageous to extend that.

COMMISSIONER PERRY: I wonder if I might suggest that you correct one statement you made which I am sure was an inadvertence; gift tax is deductible from the estate. Is it not a credit against the estate tax?

MR. GRAHAM: If you have a case of a man who knows he is suffering from a terminal illness he will make a substantial gift, let us say a man who has an estate of half a million dollars and he will make a gift to-day of $300,000.00. He is not liable to pay gift

tax until next April. If the payment is deferred then it is not allowed under the Ontario Succession Duty Act. He does, however, make the gift to-day and pays the tax to-day and that thereby comes out of his estate and effectively reduces the estate for succession duty purposes.

COMMISSIONER PERRY: There is a direct deduction allowed for gift tax.

MR. GRAHAM: So there is no possibility of increased liability to the Dominion Government and he reduces his liability to the Provincial Government.

COMMISSIONER PERRY: That is one of the satisfactory situations where we are both right.

THE CHAIRMAN: The next item Federal-Provincial Secretariat, has there been something like this proposed already?

MR. GIBSON: There has been a good deal of discussion. When we first proposed it there had not been anything like the amount of discussion on this question.

THE CHAIRMAN: The Premier of Manitoba proposed a Federal-Provincial Economic Council which seems to me the same thing you are recommending.

MR. GIBSON: The basis for our recommendation was the feeling that the problems faced by the Provinces and the Federal Government in taxation are of such a nature and so complex that it is very unlikely that the desires and wishes of the Provinces and the Federal Government will be implemented in tax legislation that will work out in the best interest of the taxpayers generally across the country.

THE CHAIRMAN: I was not quite clear whether you would be restricted to economic and fiscal matters or go beyond that to social and other matters.

MR. GIBSON: Economic and fiscal matters originally was our thought, making a civil service body that would effectively take into account the desires and wishes of the Provinces as well as the Federal Government and try to propose forms of taxation that would accommodate both parties.

THE CHAIRMAN: I would have thought if we are to use some of our fiscal measures for economic purposes there must be the closest co-operation between the Federal and Provincial Governments.

Perhaps this is the way to do it. It is beyond our job but we are interested.

4 We have no more questions. I would like to repeat that we are grateful to you for this day. It has been very helpful to us and contributed very much to our task -- I was going to say "the ease of our task" -- but we haven't got to that point!

MR. GIBSON: Thank you very much indeed, Mr. Chairman and members of the Commission, for giving us such a careful hearing.

THE CHAIRMAN: Mr. Secretary, we will stand over until 9:30 tomorrow morning.

---The hearing was then adjourned until 9:30 A.M. December 4, 1963.

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# ROYAL COMMISSION

ON

# TAXATION

## HEARINGS

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# THE ROYAL COMMISSION ON TAXATION

Hearing held in the Centre Court Room, Exchequer Court of Canada, Supreme Court Building, Wellington Street, Ottawa, Ontario, on Wednesday, the 4th day of December, 1963.

## C O M M I S S I O N

MR. KENNETH LeM. CARTER — CHAIRMAN

MR. J. HARVEY PERRY

MR. A. EMILE BEAUVAIS

MR. DONALD G. GRANT

MRS. S. M. MILNE

MR. CHARLES WALLS

## LEGAL COUNSEL

MR. J. L. STEWART

## RESEARCH DIRECTOR

PROF. D. G. HARTLE

## SECRETARY

MR. G. L. BENNETT

* * * * *

## INDEX TO EXHIBITS



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---Upon commencing at 9:30 A.M.

THE CHAIRMAN: Mr. Secretary, are you ready?

THE SECRETARY: Mr. Chairman and Commissioners the first brief this morning is being presented by the Canadian Electrical Association. Mr. B. C. Fairchild, General Manager of the Association is here this morning. He will make a few opening remarks and introduce his colleagues who are with him.

I will enter this brief into the record, Mr. Chairman, as Exhibit 277.

---EXHIBIT NO. 277: Brief of the Canadian Electrical Association

SUBMISSION OF

CANADIAN ELECTRICAL ASSOCIATION

Appearances:
Mr. B. C. FAIRCHILD, General Manager, of the Association
MR. J. M. HAMBLEY, General Manager of Ontario Hydro and Senior Vice-President of Canadian Electrical Association
MR. D. A. HANSEN, General Sales Manager of Calgary Power Limited and President of Canadian Electrical Association
MR. A. C. HOWARD, Vice-President of Montreal Engineering Company.
MR. D. C. CAMPBELL, Assistant General Manager of Canadian Electrical Association.
MR. S. CYTRYNBAUM, Economist.

THE CHAIRMAN: Good morning, Mr. Fairchild. We have read your submission with considerable interest I may say. I would be grateful if, in commencing, you would introduce your associates to us, and add any remarks you care to make.

You do not need to read this submission as we have already done that. We will have questions we want to put to you.

I introduce to you our Commissioners whose names are all here before you.

MR. FAIRCHILD: Mr. Chairman, on my far right is Mr. J. M. Hambley, Senior Vice-President of our Association. Next to Mr. Hambley is Mr. D. A. Hansen, General Sales Manager of Calgary Power Limited and President of our Association. On my immediate left, Mr. S. Cytrynbaum, Economist from Montreal, Next to Mr. Cytrynbaum, Mr. A. C. Howard, Vice-President of Montreal Engineering Company and Past President of our Association. Beyond him, Mr. D. C. Campbell, Assistant General Manager of the Canadian Electrical Association.

Now, insofar as introducing our brief is concerned, I have one or two very brief remarks to make in that respect.

The Canadian Electrical Association was organized in 1891 and incorporated by Letters Patent under Dominion Charter in 1922.

The objects are to advance in the public service the art and science of the generation, transmission, distribution and use of electricity and for this purpose the Association has established Sections and Committees who hold meetings to discuss problems, exchange information, and hear papers pertaining to our objectives.

Corporate membership is composed of forty-four provincial and investor-owned electric utilities. Fifty-two manufacturers of electrical apparatus, equipment and appliances, 1450 individual and 280 Affiliate and Associate members.

The object of our Brief is to contribute to the determination of sound tax policies and practices, using particularly the experience and knowledge of the Association's electric utility members. We feel that the criteria of sound taxation policy should be the promotion of efficient economic growth, a fair distribution of the tax burden, and relatively simple administration and interpretation of the tax laws.

A tax exemption for electric utilities would, more than in any other industry, stimulate efficient economic growth. The tax saving would of necessity be reflected in lower rates which would reduce costs and stimulate the creation of new industries.

Now, I quote from the Royal Commission on Canada's Economic Prospects, March, 1957, in which it states:

> "For every dollar spent on construction... (in the electrical industry) two dollars have gone into the building and equipping of new manufacturing plants. For every employee engaged by the power companies, fifty have found jobs in secondary industry, and for each additional outlay on electric power as a cost of production, the nation's output of manufactured goods has increased a hundredfold."

With a view to effectiveness and consistency in tax policy we recommend the following:

(a) That the Excise Tax Act be amended to exempt from the sales tax, purchases by electric utilities of

construction material, machinery and apparatus used in the production of electricity, and all fuels.

(b) That the Income Tax Act be amended to exempt from Federal income tax those electric utilities which are presently subjected to that tax.

That is our statement, Mr. Chairman, and the gentlemen with me here I think are prepared to answer any questions which you might wish to put.

THE CHAIRMAN: Thank you very much, Mr. Fairchild. Before getting to the matter of taxation, it would be interesting to us I think to understand fully your Association and your industry. When I read your submission I was interested in the broad membership which your organization contains.

In certain matters I can understand that the interests of some of these members would be common, but I was wondering if that is true when it came to taxation, because I see some of your members are manufacturers of equipment, and it would seem to me that if the generators of power are relieved of certain taxes, it is going to put taxes on everybody else, and I would have thought they would have recognized relief to one is a burden to the other.

MR. FAIRCHILD: I think, Mr. Chairman, in that respect I might explain that our corporate membership is composed of both utilities, privately and publically operated, and manufacturers, and the manufacturers have representation on our Board of Directors.

Those representatives on our Board of Directors have seen this brief, and have said they have no objection to it.

Now, insofar as your question is concerned, I believe that we feel that the reduction of tax, effective tax on production of electricity, would increase activity in the electrical manufacturing industry.

THE CHAIRMAN: And this would be to the benefit of suppliers?

MR. FAIRCHILD: Yes.

THE CHAIRMAN: You point to the economic benefits flowing from the production of electricity. I was curious as to just how local that might be and how quickly it develops. I think one illustration is the lower St. Lawrence where at the present time there is an increase in generation facilities, I believe, and I presume that will attract industry there.

MR. FAIRCHILD: That is the intention, I believe, Mr. Chairman, of the Hydro Quebec policy in increasing availability of electricity in the Lower St. Lawrence, and they have reduced the rates in the Lower St. Lawrence with the idea of attracting industry to that area.

THE CHAIRMAN: In that effort to attract industries, has there been any evidence of success?

MR. FAIRCHILD: I would not say there is any evidence of success that I am aware of at the present time, but I believe there is a very definite effort being made to stimulate industry.

THE CHAIRMAN: Take another example. Kitimat.

It was intended to attract industry over and above aluminum. Has that succeeded in doing so?

MR. FAIRCHILD: Perhaps Mr. Howard could answer that.

MR. HOWARD: I can't answer that.

THE CHAIRMAN: I would like to get an idea as to just which is the chicken and which is the egg. It seems to me here if you set down generating facilities, industry is encouraged and develops.

MR. FAIRCHILD: I think that is true in the Arvida area, for instance.

THE CHAIRMAN: Are there any more places? I would think it would be true of the Arvida area, but that is over quite a period of time and it developed slowly.

MR. FAIRCHILD: Yes. If I may speak for Mr. Hambley's territory, the Niagara Pennninsula.

MR. HAMBLEY: I would like to go back to Arvida. You mentioned Kitimat. I think Kitimat is an outcome of the development of industry in the Arvida area. In other words, the Aluminum Company started there with the supply of electricity, which was quite adequate for its aluminum production and operation, and industry moved in which was able to pay more for electricity than the aluminum production, and the ultimate result was that Aluminum Company moved up into the hinterland for its aluminum production, and distributed its electricity to other industry in the Arvida area.

THE CHAIRMAN: Electricity very definitely attracted industry to that area beyond aluminum?

MR. HAMBLEY: Yes.

THE CHAIRMAN: I can see that pulp and paper was attracted there, but that was partly electricity and partly forest resources.

MR. HAMBLEY: There is a very heavy chemical industry in Arvida.

MR. FAIRCHILD: And down along the St. Lawrence, heavy chemical industries as a result of the Shawinigan Power Companies down there. There is a big development of both chemical and pulp and paper. Of course the source of their supply is there, but also the source of comparatively cheap power as well.

MR. HOWARD: I think in most cases the industry and power tend to go along step by step. As more power is built, the more industry is built.

THE CHAIRMAN: As I read your brief, I was inclined to form the impression that if one developed power in a certain area, industry would spring up, and I was seeking to test that. I thought that may be an exaggeration within my own mind, and it probably requires other things along with electricity.

MR. HANSEN: I think that is true. The part that electricity plays in manufacturing I think is a real part of attracting industry to the hinterland. It attracted aluminum to Kitimat; it attracted aluminum to Arvida, and the alternate is to transmit power to industry in compensation or in an offset of the transportation of manufactured goods, but where there is a high content of power required, then the industry will go where that content can be obtained at the very lowest cost.

THE CHAIRMAN: If I remember correctly, aluminum went to Kitimat and to Arvida because of two factors; one being power and the other being access to the sea. Am I not right?

MR. HANSEN: That is right, sir.

THE CHAIRMAN: Has there not always been something else along with it?

MR. FAIRCHILD: The Aluminum Company could have been a lot closer to the sea than they are in Arvida. I think they took Arvida because of the power facilities.

THE CHAIRMAN: Yes, but they would not have picked Arvida if it had not had access to the sea.

MR. FAIRCHILD: That is quite true. Another new industry, as Mr. Cytrynbaum has just pointed out to me, Reynolds Aluminum opened up at Murray Bay, and there is a good supply of power along there, coming right along that shore, and the Reynolds Company are opening up a plant for the production of aluminum cable at Murray Bay, and would be taking advantage of the fact that there is lots of power along that shore.

THE CHAIRMAN: What distance is it now economical to transmit electrical power?

MR. FAIRCHILD: It depends on the price you get for your power. Perhaps Mr. Hambley could answer that.

THE CHAIRMAN: There must be a point at which industry is encouraged to grow by the proximity of power. If they go too far away, I presume the costs go up?

MR. HAMBLEY: The practical distance depends --

well, first, it is cost of generation at the site. If it is very low, then you can spend more on transmission and still be competitive with alternative methods in producing electricity. There is much talk at the moment of sending power from Hamilton Falls to New York City, which is a thousand miles. I think there is no like transmission to my knowledge at the moment.

MR. HOWARD: I think the longest lines in the world are operating in the Soviet Union between Volga River Plants to Moscow, which I believe is around 500 miles and now operating 500,000 volts.

THE CHAIRMAN: Of course the farther you go the greater the cost because of the cost of transmission facilities and also because of the losses I would suppose.

MR. HOWARD: That is a factor, that is true.

THE CHAIRMAN: I was struck by the fact which is indicated at page 8 of your submission that Norway produces more kilowatts per capita than does Canada or the United States. I thought I found somewhere else in your submission an indication that the standard of living is generally proportionate to per capita production of electricity.

If so, I must say I would not like to swap that of Norway for the U.S.A., and I was curious as to whether or not this was a contradiction. Am I right there?

MR. HAMBLEY: I think, sir, this is a case where these averages sometimes do not provide a proper picture. I think in the case of the U.S.A. there are

areas in the U.S.A., for instance, where the consumption is well over 10,000 kilowatt hours per capita. Also there are other areas where the consumption is very much lower than the average, and where the standard of living is very much lower than that which we normally attribute to the U.S.A.

MR. HOWARD: I think the Norway figures are quite badly distorted by the electrical chemical industry in Norway, so that you do get a distorted average.

THE CHAIRMAN: It really has not as much to do with consumption, that is the consumption in the country by individuals, as it has to do with production?

COMMISSIONER WALLS: It could be the same type of distortion in Paragraph 20 where you say "even now consumers in this country are paying up to 50 per cent more for all forms of energy than consumers in the U.S." This "up to 50 per cent" could be just an isolated area in a remote part of the country.

MR. FAIRCHILD: This refers to all forms.

COMMISSIONER WALLS: I noticed that. I thought first of all that you were just applying it to electricity until I read paragraph 23.

THE CHAIRMAN: In paragraph 23 you say that we get cheaper power in Canada than anywhere, and in paragraph 20 it seems to indicate we pay more.

COMMISSIONER WALLS: It is for all energy we pay more.

THE CHAIRMAN: I think that is still a contradiction, for somewhere else I find that most of our energy is supplied by hydro electric power.

MR. FAIRCHILD: This is taken from that report that I referred to in my opening remarks, the report of the Royal Commission on Canada's Economic Prospects, March, 1957.

THE CHAIRMAN: Of course you still do not answer the question when you say you are paying up to 50 per cent more. That place where we are paying 50 per cent more for energy might just be an isolated case; is that not right?

MR. FAIRCHILD: That is true.

COMMISSIONER WALLS: Really that statistic does not mean very much.

MR. CYTRYNBAUM: May I interject that I do not think -- well, the 50 per cent figure is not our calculation. It is borrowed from the reference to the Davis Book on the Royal Commission on Canada's Economic Prospects. It includes all forms of energy, and I would guess that there are forms of energy in Canada which do cost up to 50 per cent more than they cost in the U.S.

COMMISSIONER WALLS: But that does not mean that the overall average in Canada is 50 per cent higher than in the United States.

MR. CYTRYNBAUM: No.

THE CHAIRMAN: Surely the average of all energy in Canada must be fairly low if 140 billion kilowatt --

MR. HAMBLEY: Electricity does not provide a truly large percentage of total energy used in Canada because when you think of total energy used in Canada, you think of every automobile on the street and so on.

MR. HAMBLEY: Electricity does not provide a truly large percentage of the total energy used in Canada because when you think of the total energy used in Canada you think of every automobile on the street and so on.

MR. FAIRCHILD: You might refer to Appendix B-1. You see the relative price of fuel and power for Canada and the United States -- coal, oil, electricity, and natural gas. It would seem perhaps to some extent evident that the price for coal in Canada is so much higher that brings the energy costs up.

COMMISSIONER WALLS: As far as oil and natural gas we are now running pretty close to them.

MR. FAIRCHILD: On electricity you may notice it is considerably lower. The domestic rate for electricity is about 1.64 here against 2.5 in the United States. It is quoted here somewhere.

COMMISSIONER WALLS: There is another statistic you quote and that many people have quoted who have appeared before us. It appears in the summary also on Page 12 where you talk about for every employee that is directly employed in the industry there are 50 employees in secondary industry. When Imperial Oil were before us they had a statistic which showed 40 per cent of the entire labour force were occupied in secondary occupations to agriculture.

The point is when you get into secondary occupations there are duplications otherwise you have several hundred per cent. Really the figures of the amount of people you employ in secondary industry is

never too accurate as a means of comparison with other industries. Do you agree with that?

MR. CYTRYNBAUM: Yes. I think my own need is to try and look at the whole economic question. As we pointed out on Page 9, I refer you to the report, we refer to the report of Professor John Dales where he strives to analyse the economic development particularly of Central Canada. On careful examination he concluded the two necessary factors to the economic development of Central Canada were hydro electric power and agricultural resources.

This type of analysis I believe we must be concerned with. We can find any number of inter-relationships in any conceivable industry in the country. I think we are getting to the heart of economics when we talk about the hydro electric industry. Even electric power alone is not sufficient to build an economy but it is the type of thing one cannot do without and the type of product which when available other things can start to happen.

THE CHAIRMAN: I think I will move on unless you have anything else. Now I am curious and perhaps you gentlemen can tell me why electricity was exempted from sales tax. I think you put it on the basis of it being essential and if it were taxed it would be regressive. The distinction between essential and non-essential is a very difficult line. I am not at all clear and if one exempted all those things which everybody claimed to be necessity there would be no sales tax left, or virtually no sales tax left. I would think electricity

is a pretty good thing to tax as against the consumer. Do you know why it was omitted?

MR. FAIRCHILD: If you did tax electricity, which is paid almost directly by the consumer, then you are increasing the cost of a product which we suggest if the cost is kept down will assist in a higher efficient economy in the country.

THE CHAIRMAN: Let me qualify my question to individual consumers, drawing a distinction between producers and consumers. I again say why was electricity exempt from individual consumers, from the householders and so on, rather than producers? I can understand your argument with regard to producers. It puts up the cost of production and makes our goods less competitive in world markets, but as to the consumers that does not apply and actually it is the individuals who bear the burden of taxes. It is just a question of how it gets to them.

I would have thought if they were going to spread the cost of Government this would be one good way to spread the cost to individuals. I am not talking about producers. Everybody uses it and it is a broad base we are looking for. We are looking for a further basis on which to place tax.

Everybody says to us you must recommend a reduction of taxes. That can only be done if you can find another place to put them. We are interested in that. I wanted to know why was it exempted as far as individuals are concerned?

MR. HANSEN: During the War you will recall

there was a tax on electricity at the consumer level.

COMMISSIONER WALLS: I was going to point out that on page 2 of your summary you state that Government policy has already recognized the special role of electricity in the economy and has exempted the sale of electricity from sales tax.

One form of Government has so far but there are three provinces, I believe, who are charging sales tax to the consumer on electricity. Am I right?

MR. CYTRYNBAUM: We thought we ought to restrict ourselves to the Federal Government.

THE CHAIRMAN: He is thinking of our terms of reference when he says that.

MR. CYTRYNBAUM: If I might try to continue the discussion or answer the question. Within the field of the price of electricity for the individual domestic and foreign consumer the Commissioners and the Government will have to set a series of criteria on what sort of guide line to use in taxation policy. I would think one of the criteria which we suggest is within what we call the social criteria taxation. The idea that the tax burden should be spread in such a way that those least able to pay should have the smallest burden of taxation.

We affirm the principle of a progressive taxation and within the field of taxation on electricity for consumers perhaps it is a valid judgment to say it is a necessity or not a necessity. I think some of the figures that we indicate would make us realize electricity is something everybody uses and something

which at the consumer level would be regressive. If something were put in there, for example if types of electrical products -- and this is not in the brief it is nearly a personal hypothesis -- if luxury electrical appliances, which are high users of electricity, were taxed this would not be progressive. I think that taxing electricity by the consumer per se would be regressive.

THE CHAIRMAN: Compensation is probably found in income tax. It is always acknowledged that income tax is progressive. I think one must be concerned with the total of tax. Whether the total is regressive or progressive I don't know. We will do our best to find out.

You are basing your case entirely on the regressitivity of a tax on electricity.

MR. CYTRYNBAUM: That is one of the factors.

THE CHAIRMAN: Let us have the others.

MR. CYTRYNBAUM: There is, I think, even on the consumption level something of an induced industrial effect by lower electricity rates and the higher purchase of certain types of electrical products, hence an economical development affecting that basis.

THE CHAIRMAN: Low cost encourages the development of the consumption of electricity.

MR. CYTRYNBAUM: Yes. There is no doubt that in certain areas of the country electricity is very high and a great number of the products which we generally consider bought and used by everybody are not used by areas with the high cost.

THE CHAIRMAN: The highest cost in Canada probably is in British Columbia and the use of expensive gadgets is as evident in British Columbia as everywhere else.

MR. CYTRYNBAUM: I don't think it is fair to sweep across the provinces. I am more familiar with the province of Quebec. I realize that we have low rates of electricity in certain areas and also areas where the rates are exhorbitantly high. In those areas there is a low standard of living and the cost of electricity being what it is certain types of products are not used.

You cannot isolate these areas.

COMMISSIONER WALLS: Is not the reverse also true? If you grant an exemption on electricity then that tax burden has to be paid by the consumer in some other way and they have that much less to buy electrical fixtures to use electrical energy.

MR. CYTRYNBAUM: We recognize that by lowering the tax in one area and exempting taxation from one industry at least in the short-term you will have to replenish these tax losses from other sources. What we did affirm is that at least in a reasonable short term, or if you wish in a long term, a tax policy which benefits an industry like electricity will have a beneficial effect and will increase productivity and efficiency and will increase production and employment in areas where they should be increased.

We do recognize there is the possibility of a short-term loss in tax revenue. We recommend that

this type of policy is still worthwhile and even in the short run that the tax should be garnered in those areas where it will do the least harm, not those areas where it may do the greatest harm. We might suggest some areas where perhaps the tax could be extended.

This again is a personal hypothesis. I would suggest a sales tax on all finished products at the retail level provided the proper increments be included.

This perhaps may be a good way of altering the present means of collecting money by sales tax, if sales tax was a good way of doing it, and by increasing the income perhaps by extending the services that are not now taxed.

We feel it is just as important to recognize exemptions where they are warranted. Exemption is not a tax evil. Exemption should be as much a part of the policy as application of the tax in other areas.

THE CHAIRMAN: We are interested in what you say particularly in regard to another proposal put to us. You recommend here, and it was also recommended elsewhere,,that investor-owned utilities be free of income tax. If that were done that tax has to be made up some where. One way of making it up would be to impose a tax on the consumption of electricity.

MR. HOWARD: As we stated in the beginning, Mr. Chairman, the composition of this Association is rather mixed. It contains both publically owned and privately owned sectors of the industry and also the manufacturing. I quite realize the point you are making.

I think the private companies independently have submitted briefs to you from time to time more or less making that suggestion. I think in our positionhere to-day that it would be quite inappropriate for me as a member of this Association to suggest how some other member of our ASsociation should be taxed in that regard.

THE CHAIRMAN: I can fully understand and sympathize with your position. I don't want to push you into a discussion. It seemed to me when we were discussing exemption of sales tax I should be frank and tell you what is in our mind.

MR. HOWARD: I think our submission in the brief was related to the discrimination which exists between the two sectors of our industry, and of course within our association, whereby one sector pays more of the cost of central government as against another. We are suggesting that discrimination be removed.

THE CHAIRMAN: Very good. We will let it rest there if you would like to do so and I guess you would.

MR. HAMBLEY: I believe this is a relatively insignificant amount.

THE CHAIRMAN: In your brief you say there remains investor-owned companies 15 per cent and that is delivered at a cost of 13 per cent more to consumers than the publically owned, which 3 per cent is amount of income tax contained in the bills rendered against the consumers of investor-owned hydro energy.

MR. HOWARD: On a quantitative basis I think

the present amount of tax paid by the privately owned sector is about twelve million dollars of which, I believe, the Federal Government keeps approximately one-half or six million.

THE CHAIRMAN: YOu speak about your own area. There are other areas of regulated public utilities which are in somewhat the same position, I think.

Part is supplied publically and part of their product is supplied by the Government. There is discrimination there, too, to the same extent.

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COMMISSIONER WALLS: In your whole industry you are paying a very limited amount of taxation in comparison to other industries; is that not right?

MR. CYTRYNBAUM: It is not the amount, it is the consequence of whatever is paid. I think we have established clearly whatever is paid in taxes in our type of industry is of necessity reflected in equal amounts in tax rates because of the nature of ownership and control of the industry.

We tried to establish that any increase in these rates has a type of effect that we tried to show on the whole.

MR. FAIRCHILD: Referring to sales tax, Mr. Walls, Item 56, on Page 17, you will note that the ratio of investment to revenue is relatively 325 per cent higher for electrical utitlities than for the average Canadian company. That is a tax burden because of the ratio of investments to revenue.

COMMISSIONER WALLS: But who actually pays the tax?

MR. FAIRCHILD: The consumer pays it.

COMMISSIONER WALLS: So therefore it doesn't really make much difference which way he pays it. Branching away from that, I think you have a justifiable claim that with respect to an exemption for diesel fuel even although the Government may have said before, it was too administratively difficult to decide the end use. They already have many exemptions for different uses on which they allow it on diesel fuel that I think your case if justified.

They are also applying like exemptions to fasoline. For instance, it applies to testing of motor driven equipment.

I think there are so many exemptions that your case should not be put aside from the standpoint of being administratively difficult any more.

MR. FAIRCHILD: I would like to point out in connection with diesel fuel tax this affects a number of relatively small utilities who are operating diesel plants, and they seem to be picked on because of the fact that they only have small consumption in the area which only requires, comparatively speaking, a small diesel plant, and the type of plant which could only be used for that particular load.

COMMISSIONER WALLS: I think they have just as good a case as the mines who manage to get it tax free for generating electricity in mines.

MR. FAIRCHILD: We have appealed to the Minister on three different occasions prior to each budget -- before the last three budgets that have been issued -- in this respect.

MR. HANSEN: Does that bring up a point of degree of sensitivity in areas and sources? The area that has to rely on that type of generation, then that is sensitive; where another area is relying on hydro or themal from another fuel, then they are not sensitive to that particular point.

COMMISSIONER WALLS: It seems to me we heard a claim from a like industry for exemption on natural gas being used for this purpose and the natural gas use was not for a backwoods small unit.

MR. HANSEN: I think that was whether it was a gas turbine or gas engine.

THE CHAIRMAN: I understand that all of your equipment in construction is now subject to sales tax. Am I correct? All capital expenditure in generation.

COMMISSIONER WALLS: Some of it is subject to 11 per cent and others are subject to the 4.

THE CHAIRMAN: I am accepting that, yes. What is requested here is exemption of all of that whole area from sales tax? I would think the amount involved would be pretty much because it would be 11 per cent and 4 per cent of the total expenditure.

MR. HOWARD: Along with what you are saying, I think the effects of sales tax of course on capital industry such as ours are very high. I might say recently we estimated the cost of building a large steam plant amounting to some thirty odd million dollars, and the effect of the sales tax at the 11 per cent level was to increase the cost of that particular project approximately eight and three-quarters per cent.

THE CHAIRMAN: Why not 11 per cent?

MR. HOWARD: A certain amount of it is labour, and the cost of labour and labour of erecting machines is not taxed.

THE CHAIRMAN: All capital expenditure in your industry it can be assumed costs something like 8

per cent more because of sales tax than it would cost if your recommendation were accepted? Am I right?

COMMISSIONER WALLS: Just one second. He is also including sales tax on building products too in that, are you not?

MR. HOWARD: I was including sales tax on building products. The amount of building products as such, is relatively small, compared to machinery costs.

THE CHAIRMAN: That would be true throughout I would assume.

MR. HOWARD: Yes, I would think so to more or less a degree. In distribution, for instance, I would think the labour component would be considerably higher than in power generating plants, so that the effect of the tax would be somewhat lower in the case of tramsmission and distribution.

THE CHAIRMAN: So that the effect of your recommendation is something less than 8 per cent?

MR. HOWARD: Something less than 8 per cent.

THE CHAIRMAN: It is something less than 8 per cent of the total amount spent on facilities for the generation of electricity by hydro; is that right? That is the substance of what you recommend to us?

MR. HOWARD: Yes, yes. We have not made a specific test on the water power plant, but I would assume that it would be probably less than 8 per cent with the larger component of labour and other works going into a water power plant.

MR. FAIRCHILD: You are probably aware power companies were previously exempted on production machinery,

and now the tax has been slapped back.

COMMISSIONER WALLS: On production machinery it is in all industry. That is why I am rather surprised with your asking for it your industry only.

MR. FAIRCHILD: We felt with our industry being, as we have mentioned on several occasions, responsible for the economic efficiency of the country, exemption for our industry would have a bigger effect than it would for others. But perhaps we are patting ourselves on the back to that extent. Nevertheless, we feel we are an important industry.

THE CHAIRMAN: What would the effect of that be in terms of your product? What proportion of the sales value of your product is represented by capital expenditure?

MR. HAMBLEY: I can only answer it by saying that the cost of carrying our capital is in the area of 50 per cent of our total cost. Whether that is an answer or not.

THE CHAIRMAN: Yes, I would think so. If your capital costs are half of your total costs, can we not assume that half of your revenue costs would be capital costs?

MR. HOWARD: I would be inclined to agree with what Mr. Hambley had to say.

THE CHAIRMAN: So if it is something like 50 per cent instead of 80 per cent, we will say, your capital expenditure after sales tax, the effect of that on your product would be 50 per cent, would it not?

MR. HOWARD: It would be of that order, yes.

THE CHAIRMAN: I was looking for some kind of relationship. Have you anything more on "electricity and the sales tax"?

COMMISSIONER WALLS: No, I don't think so except the fact in dealing with this question of the Minister, you state that you are generally permitted to go to the Tariff Board, and you also have power to go to the Exchequer Court, do you not, as well? On a point of law you can go right to the Supreme Court, so there isn't quite the restriction you claim. About all you have from the Ministerial end and eventually the Tariff Board end, if you want to, is purely a matter of interpretation. Am I not correct?

MR. HANSEN: Yes.

MR. CYTRYNBAUM: A Minister to have final discretion.

THE CHAIRMAN: A very wide area where the Minister makes the decision and there is no appeal from that to the Tariff Board or anywhere else, is there? I thought that is what you were referring to.

MR. FAIRCHILD: Perhaps there is something I am thinking of that may be of assistance in that respect. We had a lot of experience with respect to the tax exemption on production machinery when that was allowed, and in many cases, many, many cases, we would have to go to the Deputy Minister to find out whether he would agree such and such a piece of equipment was classified as production machinery in an electrical generating station. It was practically left to his discretion as to whether we got an exemption or did

not get an exemption and we had lots of arguments with him. "No, that is it", so I was led to believe that was the end. We couldn't get any further than that. The Deputy Minister decided that was it, and that was it.

THE CHAIRMAN: I do not think that is the end. I think if you looked up your law you would have seen there is a right of appeal. As far as I know that goes back a long time.

COMMISSIONER WALLS: Yes.

THE CHAIRMAN: And you can go, as Mr. Walls said, to the Tariff Board. It is in a different area where discretion lies with the Minister but not in the matter of classification.

We move on to "electricity and the corporate income tax". I was interested in your statement to the effect the electrical utilities in Canada pay relatively 565 per cent more in income than the average Canadian corporation. I think I questioned that statistic. I think the statement merely means that in your sales dollar there is 565 per cent on what the income tax is in the average sales dollar everywhere else in Canada.

MR. HOWARD: I believe that would be the interpretation.

THE CHAIRMAN: I do not think that is quite what you say here because your income in proportion to the investment dollar in your industry would be the same as what it would be throughout the land I would expect, or approximately so. You are tying it on the sales dollar here.

MR. FAIRCHILD: You see on Page 41, appendix

D-1, the relation of income tax to revenue and the ratio of investment to revenue.

THE CHAIRMAN: 13.3.

MR. FAIRCHILD: That is right, sir. Incidentally, that percentage figure on the next column should not be in there. That is ratio of investment to revenue and is not a percentage figure.

THE CHAIRMAN: Right. I am sorry I missed a question by moving on a little too fast. Mrs. Milne has one on Page 14.

COMMISSIONER MILNE: In respect to Paragraph 41, I thought perhaps Mr. Cytrynbaum might be able to give us a breakdown of detail that is in appendix C-1 which deals with food, housing and fuel as items that form the greater portion of total expenses of low-income groups in comparison to high-income groups.

In appendix C-1, the percentages are underlined, and certainly housing, fuel, light and water are definitely high. I would have thought housing and fuel would form a greater portion of those percentages, and I was wondering if in your preparation of the brief you had details that would suggest to what degree electricity formed part of those totals.

MR. CYTRYNBAUM: These figures are taken directly from D.B.S.

COMMISSIONER MILNE: Yes, I noticed that.

MR. CYTRYNBAUM: And we were unable to get a further breakdown. I assumed that in putting these figures together there would be some sort of co-relation and some meaningful data for D.B.S. to put them together.

I regret I have not got that.

COMMISSIONER MILNE: I noticed they came from the D.B.S. figures. I thought since it was your own statement in the brief possibly you did have details in respect to electricity.

MR. HOWARD: I think there is such a breakdown in the United States. If you are interested, I think we might obtain that for you.

COMMISSIONER MILNE: I think it might be interesting; certainly to me, because I am particularly interested in the different income groups.

MR. FAIRCHILD: Would you like to have the effect on various income groups that the cost of electricity might have on them?

COMMISSIONER MILNE: Yes, also I possibly felt it might be extended to appendix C-2 if there was something there you could substantiate.

MR. FAIRCHILD: C-2 is a straight statement of average dollar expenditure per family. Would you like that broken down also into various income groups?

COMMISSIONER MILNE: Yes, but I do not know that that has as great a bearing. I am particularly interested in this, but nevertheless I do think it was brought up this morning by Mr. Cytrynbaum that in certain provinces possibly more electrical equipment is used and greater energy is used, and possibly these too would vary.

THE CHAIRMAN: C-3 is the same problem as you raised with C-1, is it not?

COMMISSIONER MILNE: Yes.

THE CHAIRMAN: I'm not sure that C-2 is.

COMMISSIONER MILNE: No, C-2 is another problem.

THE CHAIRMAN: It would seem to me C-3 is the same thing as you raised in C-1.

MR. FAIRCHILD: We will see if we can get a breakdown of these figures in C-1, 2 and 3 in relation to family income.

THE CHAIRMAN: I think that would be very interesting to all of us.

MR. FAIRCHILD: Incidentally, we had quite a time with the Dominion Bureau of Statistics for many years. They insisted on including the cost of coal oil with the electricity. We finally convinced them people weren't using coal lamps any longer.

THE CHAIRMAN: They got figures for electricity --

MR. FAIRCHILD: They have index figures for electricity, yes.

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MR. FAIRCHILD: The index figure for domestic electric consumption to-day in relation to 1949 -- 100 is 116 today.

THE CHAIRMAN: With regard to this last section really the important recommendation is contained in your paragraph 67 recommending that the Federal Government vacate the field of income tax on regulated public utilities. I guess you are restricting it to the Hydro Electric because that is what you are speaking to us about.

MR. FAIRCHILD: Investor-owned electrical utilities.

THE CHAIRMAN: You would leave the Provincial Government in that or are you not speaking for them.

MR. FAIRCHILD: We are speaking for the Provincially-owned power systems, the members of our Corporation. In this instance we are speaking of the investor-owned.

THE CHAIRMAN: That is not my question. The words I have in mind are "for the Federal Government to vacate this field." Should I read that "the Federal and Provincial Governments to vacate this field" because they levy income tax on public utilities, do they not.

MR. HOWARD: We are suggesting the Federal Government vacate the field insofar as the investor-owned utilities are concerned and leave the question of taxation to the provinces themselves, whereas the discrimination between provinces would be removed.

THE CHAIRMAN: The issue is really caused by the Federal Government taxing. It has nothing to do

with the Provincial Government's taxing.

MR. HOWARD: The problem generates from the question of takeovers.

COMMISSIONER WALLS: Is not the alternative to tax all provincially owned corporations and then you would all be in the same boat!

THE CHAIRMAN: I really said I would not provoke them into discussion because it is not fair to the membership.

COMMISSIONER WALLS: I am not provoking them. It is another alternative to the same problem they are facing. That is all.

MR. HAMBLEY: There is some difficulty in taxing the income of a corporation which makes no income.

MR. HANSEN: That opens a vast question.

THE CHAIRMAN: It is pretty easy to price out, as you say. I think that is probably all the questions we have got.

I thank you very much indeed. I don't think we have any further questions, gentlemen. You have put your brief before us in a very complete manner and I think we can understand it and continue to consider what you have said but certainly you must understand if one recommends the removal of a tax from certain people one has to find some other place to put it and we are looking at you not just having regard to what we can take off but also having regard to what we can put on, as we are with everybody else in the community.

MR. FAIRCHILD: Thank you very much for your gracious hearing.

THE CHAIRMAN: Thank you, gentlemen. We are glad to see you. We will break off for ten minutes.

---A short adjournment.

THE SECRETARY: Mr. Chairman and Commissioners, the second brief this morning is being presented by the Canadian Electrical Manufacturers Association. Mr. F. G. Samis, General Manager of the Association, together with a number of his colleagues, is here before you and they will speak to the brief.

I would like to enter the brief into the record as Exhibit 278.

---EXHIBIT NO. 278: Brief presented by Canadian Electrical Manufacturers Association.

SUBMISSION OF

CANADIAN ELECTRICAL MANUFACTURERS ASSOCIATION

Appearances: MR. W. L. GLASSPOOLE
MR. F. G. SAMIS
MR. K. J. HARVEY
MR. P. F. CONNELL
MR. H. HUGHES

THE CHAIRMAN: Thank you, Mr. Secretary. Good morning, gentlemen. Thank you for putting your names on the table there. That is a help to our failing memories. I introduce to you the Commission whose names are all here.

We have read your submission with interest and we will have some questions to put to you but before doing so is there anything you would like to say to us?

MR. SAMIS: Mr. Chairman and Commissioners, I would like to introduce, even though their names are marked here, Mr. Hughes of Canadian General Electric, Mr. Connell of Canadian Westinghouse Limited, Mr. Harvey of Burndy (Canada) Ltd., who is the Chairman of the delegation, Mr. Glasspoole of Northern Electric Limited.

We understand you have read the brief and we have no other statement to make in advance except that we are prepared to answer questions and are at your disposal.

THE CHAIRMAN: Thank you. You have indicated in paragraph 5 the low rate of return earned by your industry and I have seen this information made public over the years. This low rate of return has been going on for some time to the best of my recollection and I wonder why your industry should not come up to the national average. You are about half the national average; am I not right?

MR. HARVEY: At the present time that is approximately correct.

THE CHAIRMAN: That has been true for some years?

MR. SAMIS: For some years it has been relatively lower than other manufacturing industry in Canada but during the past six years particularly it has declined rather sharply. I don't have the precise figures here. It is difficult to get precise figures on this kind of statistic but roughly in the six years the rate of return on the sales dollar, the percentage profit on the sales dollar after tax has declined in

electrical manufacturing from a little over 4 per cent down to a little under 2 per cent in 1961 and then a little over 2 per cent in 1962. It has turned upward slightly.

During that same period of time all secondary manufacturing declined in the neighbourhood of 3.9 per cent to about 3.3 per cent so that our decline was relatively greater but there has been a general decline in secondary manufacturing.

THE CHAIRMAN: The return on the investment dollar is much more interesting than the return on the sales dollar because one makes an investment to earn a profit and that is the real test, I think.

The decline is about the same as what you speak of, am I right?

MR. SAMIS: That is a much more difficult figure to obtain and we don't have such a figure with any degree of precision at all.

THE CHAIRMAN: Can you tell me why you are lower than the national average for manufacturing? Are there any stated reasons?

MR. HARVEY: No, other than it is stated that domestic and foreign competition at the present price levels is the reason most commonly advanced and illustrated.

THE CHAIRMAN: Are you particularly subject to foreign competition?

MR. SAMIS: Yes, this industry is singularly sensitive to foreign competition. Approximately 28 per cent of the Canadian market for electrical products

is filled by import products almost all of which are of a kind made in Canada. That figure over a period of years has run that high or a little higher.

THE CHAIRMAN: It is remaining about steady?

MR. SAMIS: I would say it has declined a few percentage points over a period of a decade.

COMMISSIONER WALLS: Does this apply to all types of electrical appliances or is it principally in the line of tubes and bulbs and things of that category?

MR. SAMIS: It does fall more so in the line of tubes and electronic components and devices at the present time but this shifts from time to time.

COMMISSIONER WALLS: The larger types of electric appliances are not imported to any great extent, are they?

MR. SAMIS: Oh, yes.

COMMISSIONER WALLS: Except principally from the United States?

MR. SAMIS: Particularly from the United States.

THE CHAIRMAN: On the other side of that how much does your industry export?

MR. SAMIS: Exports have increased in past years from a figure of about 3 per cent of total production. As of the first half of this year 8.6 per cent of total production.

THE CHAIRMAN: From about 3 per cent, I think you said?

MR. SAMIS: Right.

THE CHAIRMAN: Is that due to any particular

reasons which can be recognized and stated.

MR. SAMIS: I couldn't say definitely that they could be too well identified. It is due to a combination of circumstances in my opinion, including the Government encouragement to export, their assistance.

THE CHAIRMAN: I heard it stated the other day that the Canadian Electrical Industry had succeeded in reducing the production costs of a lot of its products and they are now competitive with what we had been formerly importing so they were now competitive in the world markets.

MR. SAMIS: That is true and becoming increasingly true in some fields. As far as increasing or decreasing costs there is one figure which comes to my mind. On the output per capita per employee in the industry it has increased 43 per cent in the past decade in terms of current dollars. So that it is increasing productivity pretty substantially.

THE CHAIRMAN: Yes, I think so.

COMMISSIONER GRANT: Where is your export trade going? Is it to the United States or is it into world countries other than the United States?

MR. SAMIS: I am sorry I haven't the statistics on this but my general impression of it would be that quite a bit of it is going into the United States market. Apart from that it is going to many countries throughout the world. In total if I added them up there would be 30 or 40 countries to which members of the industry export in the course of the year.

They export to South America and to some

extent the British West Indies, some in Europe, South Africa, Australia.

COMMISSIONER GRANT: What branch of the industry is experiencing the greatest growth in export?

MR. SAMIS: I am sorry I am not prepared to answer that question off hand. I haven't studied the statistics.

COMMISSIONER GRANT: Just as a matter of interest I was asking the question. The fact you have been able to reduce cost materially do you attribute that to automation or is it more proficiency in your labour force or a combination of both?

MR. SAMIS: It is a combination of both in my opinion, sir.

THE CHAIRMAN: Moving to taxation, I observe on page 5 we start with income tax and on page 11 you say "Detailed comments on income tax". The detailed discussion with regard to administration is on page 15?

MR. SAMIS: Correct.

THE CHAIRMAN: So that if we deal with the recommendation on Page 9 as to administration your discussion is amplified on Page 15. I think that is correct?

MR. SAMIS: Correct.

THE CHAIRMAN: You recommend that the determination of taxable income should be mainly in accordance with generally accepted accounting principles.
I think we would probably all like to see our taxes based on income return as close to what we are used to if it were possible to do that but how does one achieve that?

One way is to write into the Act such a phrase as "Generally accepted accounting principles". There are pros and cons to that solution. We have heard a good deal on both sides.

Do you have any views on whether the Act should be amended? If you don't intend that in your recommendation I would like to know what you do intend.

MR. HARVEY: I think it is fair to say we would recommend that be written into the Act, yes.

THE CHAIRMAN: Then if one did that it is quite reasonable to remove from the Act the long section dealing with reserves, I imagine. Would it be possible to remove other things from the Act, do you think, to simplify the administration?

MR. CONNELL: The matter of dealing with the valuation of inventories is another section that would be considered.

THE CHAIRMAN: The valuation section is a pretty simple one.

MR. CONNELL: I think in operation it seems to run into some difficulties of interpretation. I think there is some doubt as to what the interpretation really is. For example, what is cost and what is market? This has presented some problems in assessing the taxpayers.

THE CHAIRMAN: You think if it were left to accounting principles one might remove some of the problems?

MR. CONNELL: I believe so. I believe you may also have to introduce some means of hearing, through perhaps an intermediate Board of some sort composed of people who were competent in this area to

judge differences of opinions between the Tax Department and the taxpayers.

THE CHAIRMAN: In other words, you are suggesting expertise in this area be added to the Income Tax Appeal Board?

MR. CONNELL: Yes, or you may have to have a sub-Board who would attempt to dispose of these matters rather than taking them to that point.

THE CHAIRMAN: I think perhaps valuation of inventories is the most technical difficulty one can consider in this area. Do your members feel that the denial to them of base stock or LIFO is of importance? We have heard very little about that and with the exception of the very few taxpayers I would have thought it was not important.

MR. HARVEY: I don't think this represents a particular problem to our membership. Possibly a measure of inventory obsolesence does and possibly this is the specific area of inventory valuation which we are getting at here.

THE CHAIRMAN: The obsolesence factor in the valuation of inventories?

MR. HARVEY: That is right.

THE CHAIRMAN: I would move on to No. 2 where you recommend in favour of advance rulings on specific tax matters. Now that sounds to me as though you would not intend a general system of advance ruling. You say on specific tax matters. Did you contemplate advance rulings would be given in respect of certain sections of the Act and in respect to other sections

of the Act or did you mean when one has a specific problem he could always obtain an advance ruling?

MR. HARVEY: I believe we meant the latter.

THE CHAIRMAN: You have thought about the difficulties which would be inherent in this and that if one embarked on such a plan it would probably cause the tax administrator to deny you any informal rulings because there was an appropriate channel to go to.

He would then say to you you had better proceed to that particular place and the effect of asking for a binding ruling would be it would be tantamount to assessment in advance. It would not be lightly done, it would have to be done very carefully indeed.

If there were assessment in advance I suppose it would imply an appeal with regard to the assessment and it might become a pretty formidable affair. They do this in Sweden and it is slow, it is formidable. However I think on balance the Swedes appear to like it. I am not sure we would.

MR. HARVEY: It would seem to me this represents assessment in advance but the ruling in itself, I don't suppose, would be subject to appeal. The appeal would come when you chose to take the contemplated action in spite of what the advance ruling might have indicated.

THE CHAIRMAN: It could be either way. We will move on to 2.(b): "Provide taxpayer with interpretative information relative to tax laws similar to that currently provided to the Tax Department Auditors." You believe that we are now lacking in sufficient in-

formation with regard to the operation of our tax laws, I take it.

MR. HARVEY: That is right.

THE CHAIRMAN: We don't really know very much about what is provided to the Tax Department Auditors. I don't think those books are generally available.

MR. HARVEY: This is very true indeed. I suppose what we are really thinking of is what should an audit attitude be on provisions for bad debts, inventory obsolesence, that type of thing generally. I think we are suggesting the taxpayer should be as completely informed as possible so that he can conduct his affairs on as knowledgeable a basis as possible.

THE CHAIRMAN: Is there any particular area where information is conspicuously lacking?

MR. CONNELL: I think the areas where there seems to be doubt or controversy perhaps between the Tax Department and the taxpayer is again in the areas of inventory, allowance for doubtful accounts, and Section 85 reserve type situations, so-called reserve type situations.

THE CHAIRMAN: (c) "Provide more frequent audit of taxpayers returns, preferably on an annual basis." I don't think I was aware up to now that there was a lack of frequency. What period is now customary? I understand the Tax Department in its assessments has what they call desk assessments which are done without visit and then they have visits. I suppose in some cases they visit more frequently than in other cases. Is that right? I honestly don't know.

MR. HARVEY: That is correct, I believe. I think it is fair to say as far as the larger companies are concerned, for example Westinghouse, Canadian General Electric and Northern that assessments are done or audits are conducted on a virtually annual basis on the taxpayer's premises. I don't believe this is the case as far as smaller companies are concerned.

I think maybe the feeling here is that the finalization of an assessment should not be permitted to drag on indefinitely so once again the taxpayer is operating under somewhat of a clouded situation insofar as possible tax liability is concerned.

THE CHAIRMAN: I couldn't agree with you more. Is that the practice to allow them to drag on?

MR. HARVEY: I believe this is true, yes.

MR. GLASSPOOLE: I think it pertains to the smaller corporations as opposed to the types actually represented here. This is a point which has come up. I think the attitude has been to concentrate from an assessment point of view on those areas possibly where the large revenues are coming from.

I think it is discriminatory to a point in that the little fellow has to be recognized too.

THE CHAIRMAN: I suppose if the Department were short on staff they would tend to look at the areas where the largest amount of money is invested?

MR. HARVEY: Yes, I think they take a very practical approach to it, as they must do. I believe if you vacuum the details here we have suggested, assuming it is not practical for an audit to be conducted annually

for all taxpayers, then the application of interest to any potential assessment should be restricted in the period of time that it can apply.

THE CHAIRMAN: The next item is "provide for more expeditious handling of tax appeal cases." Do they linger? I was not aware of that?

MR. HARVEY: I believe they do. I can think of one specific example. It happened to be one of our members and I believe that this particular appeal case took something like ten years to settle.

Maybe this was the exception to the rule but it would seem to me that general comments in this area, newspapers and so on and so forth, would imply that it is somewhat of a prolonged decision.

THE CHAIRMAN: Do you mean that it went to the Supreme Court and through the full course of that it took ten years?

MR. HARVEY: I cannot answer that question.

THE CHAIRMAN: Of course the Courts will take some time to complete the matter. I really thought you were addressing yourself to the procedure before it got to Court.

MR. HARVEY: No, I believe it was after it reached the Court. I could get the specific information if it is of interest to you?

THE CHAIRMAN: Yes. We have already had representations in regard to the length of time it was taking to go to the Court. I was a little more concerned in this particular instance with clearing the matter through the Department, wondering if that was unduly slow.

MR. HARVEY: No, we were not inferring that here in any event.

THE CHAIRMAN: Item 3 - Ministerial discretion. What do you mean by the words "practical application of our taxing statutes"? You say that should be kept to a minimum consistent with the practical application of our taxing statutes. Some people have told us there should be no Ministerial discretion whatsoever in our taxing statutes. They say the rules should be laid down and if there is a dispute it should be settled by a third person, not by one party to the dispute.

You would let down to the point where in order to expedite matters you would give some discretion, I assume, to the Minister. Is that right?

MR. HARVEY: That is correct.

THE CHAIRMAN: Can you think of the areas you would permit discretion? There is very little in the Income Tax Act now as you are well aware.

MR. HARVEY: That is correct. I suppose the most recent budget introduces two areas of Ministerial discretion, related companies being one and dividend stripping the other. It seemed to us that apparently it was close to impossible to prevent this type of tax avoidance, if you like, by writing it word for word into an Income Tax Act. I think it is our feeling that by all means the intent of the Income Tax Laws should be followed. If it is not practical to word them in such a fashion this type of transaction can be prevented through legalistic terminology in the Act then maybe Ministerial discretion should be permitted.

THE CHAIRMAN: Then you believe there is an area where it is impossible to ascribe the rules?

MR. HARVEY: I can only presume this is the case otherwise they would have to revise the wording of the Income Tax Act rather than introducing Ministerial discretion in these areas.

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MR. GLASSPOOLE: May I comment on Item 12. One of the main reasons for its inclusion in the brief, it is not intended specifically to be any criticism of current practice, but rather, a confirmation that we agree with the barrier that is place here. We are not being critical necessarily of what is going on to-day. We are attempting to reconfirm that the present practice should continue.

THE CHAIRMAN: I thought you were perhaps endorsing 138(a).

MR. GLASSPOOLE: Only to a minor extent. We are saying in effect that we do not feel that it should go possibly beyond where it is now.

THE CHAIRMAN: That is why I have underlined the words "practical application" because it is of grave importance to try and decide as to where it is necessary to have Ministerial discretion, and where that gets into an unnecessary area.

Some people believe that the Act might be facilitated by more Ministerial discretion, so I am indeed interested in your opinion in this matter. I am inclined to the view that you believe, that it should be kept to a minimum. Also there is the belief that there is an area where the only solution is to use Ministerial discretion.

MR. SAMIS: This is right. We believe this is a matter of principle, and we have argued this before a committee of the Senate, that there are circumstances where, if the facts had to be elicited in a public tribunal, the whole truth would not come out

because of competitive circumstances, and justice would not be done in some circumstances. Particularly this is so where there is a competitive situation that one does not wish to disclose publicly all the factors that enter into it.

We have advocated in such cases that ministerial discretion is appropriate and should be final.

THE CHAIRMAN: You think that pertains to income tax?

MR. SAMIS: Not in a very wide area, but as we have said here, we do not disagree with what is being done at the present time. This is sort of a barrier against unnecessary extension of the practice. This is the purpose of what we say here.

THE CHAIRMAN: It provides another reason for ministerial discretion which I have not heard before, namely the confidential nature of the material. What you have said before was that ministerial discretion be used were it not possible to come to a conclusion without it because of defect of writing down rules, and now you are saying possibly we should use it in those areas where the matter is somehow confidential that it should not be brought out in Court.

If I may remind you, the first Court in the income tax can be held in camera. Do you really think with that safeguard it is necessary to introduce ministerial discretion into the income tax law in order to protect the confidential nature of the material?

MR. HARVEY: I would not think so myself. I cannot conceive of a situation arising under the

Income Tax Act.

MR. CONNELL: I think it would be minimal myself. I think our concern here is to ensure that the policy of keeping this type of discretion to an absolute minimum should be continued for the future, but there may be circumstances that would indicate that this is the only practical way to effectively deal with particular situations in order to implement the intent of the law.

THE CHAIRMAN: You are going further than the Minister when he introduced 138(a) because he indicated that was a temporary expedient only. He did not believe that Ministerial discretion was necessary as a final cure I do not think.

MR. CONNELL: Presumably this is an interim measure pending his developing some other terminology to cover the situation, which he has not apparently as yet been able to develop.

THE CHAIRMAN: He has so indicated. Now, moving on to income tax and fiscal policy, I was wondering what you had in mind when you say consideration should be given to implementing such fiscal policy through some medium other than the Income Tax Act. Are you thinking about substituting something for tax holidays or incentives for research.

I would have thought perhaps the only alternative would be substitutes but there may be other ones. I am not very sure.

It seems to me this is a most important recommendation of yours where you suggest that if some

other means could be found it would provide for better accounting and would bring out into the light the cost of these things, "providing a means for determining the actual cost of such a programme in tax dollars, which cost would be essential in order to do an adequate assessment". I have often thought that one of the deficiencies of tax concessions is the fact that we do not clearly label the cost of these things. Is there not some way of showing the country what the cost is of transferring the burden or burdens of taxation from one group to the whole, because that is undoubtedly what you have in mind when you write this section? Am I not right?

MR. HARVEY: That is correct, sir. I believe we had in mind subsidies. We had no more idea than that.

THE CHAIRMAN: I suppose we have all been tossing that idea around ourselves, wondering if there is not some other way of doing it. The only other way, as I say, that I have been able to thinkof is subsidy, and perhaps that is the strong and right approach, I don't know, but I would be very glad to hear if you have developed any thoughts along the line of just how to apply it.

MR. CONNELL: It seems to me that the application would still for that matter follow the identical means of calculation as exist right now. However, again it would be by means of a repayment to the party involved. However, it is the strong feature of identifying the cost of these policies so that they

are known and have to be justified before Parliament.

THE CHAIRMAN: One could quite well wonder what the amount of tax incentive, such as accelerated appreciation ,would be in terms of its relationship with the cost of an item of plant. Accelerated appreciation subsidy of X per cent in respect of the cost of that equipment would be paid? That is what you are suggesting?

MR. CONNELL: Yes, and the rule of subsidy also might very well permit a more rifle-shot approach to particular policy problems as opposed to the shot-gun approach which advocation through the Income Tax Act tends to do. In other words, there are people who are receiving benefits who merely are receiving a windfall or gratuitous benefit.

COMMISSIONER PERRY: How far would you go with this? Would you regard the element of difference between straight line depreciation and present rates on capital cost allowance as having a subsidy effect?

MR. CONNELL: I regard the technique of capital cost allowances as being an administrative steamlining of allowance of depreciation to the taxpayer as opposed to the previous taxes.

COMMISSIONER PERRY: Yes, but it did increase rates somewhat at the same time.

MR. CONNELL: This may have been a necessary part of the simplification process. It would tend to be perhaps more generous so as not to injure some taxpayers. Of course other taxpayers might state present rates are insufficient. I wouldn't want to take any position at the moment on that.

COMMISSIONER PERRY: The real difficulty here is in the establishing of some base for what is normal beyond which anything extra is incentive or subsidy. It is the more selective special sort of thing that you have in mind?

MR. CONNELL: Yes, where one taxpayer is relieved of taxation as opposed to another taxpayer because of some specific thing that he is doing.

3 I think we did enumerate some examples here on tax holidays, streamlining ventures -- this is in paragraph 13 on Page 6 -- incentives for locating plants in certain areas, and so on. This is the sort of thing really we had in mind. We are not attempting to assess here the wisdom of these particular incentives.

THE CHAIRMAN: This is a most important area I think, and one that certainly interests me a great deal because I would certainly like to see the cost of all these incentives brought out in the Government accounts in some way. It may well be able to do it as income tax concessions. Certainly they would come out very clearly on subsidies. I am sorry that you did not come out firmly and say "We hereby recommend that subsidies be paid in respect of income tax incentives".

MR. HUGHES: I think we had subsidization in mind in this recommendation. We think it would be good for the country if these accounts were brought out instead of being so indirect as they are now, and hidden, with little accountability for them.

MR. GLASSPOOLE: I think my confreres would agree with me in one of the particular areas, namely

scientific research, there was a lot of soul searching done before this was included in the brief, and in this particular connection we are not opposed to the principles that are employed in inciting people to greater scientific research.

The problem as we see it is do we have this item under control? When one refers to the term "subsidy", or the word "subsidy" as such, there is always the tendancy of pre-approving -- the Government saying "Yes, we will approve this" before the fact, or "No, we will not approve it" before the fact.

We think in this particular case, for example, this could be harmful. We think it is in the interests of the economy at large to grant a free hand in this area, but we are concerned, as the brief indicates, that it could get out of control because of the fact that it is not indicated what it is costing the company by way of this incentive or by way of this subsidy, if you will.

At the same time we recognize that this type of legislation must be subject to very close audit, and therefore the question arises, "How do we take it out of the income tax vehicle and put it in another vehicle, possibly a brand new one, and not increase the cost of administration of the Government in ensuring that the accounts as submitted are correct?"

One of the answers that have been given in this particular area is possibly it could stay within the vehicle it is, as a separate computation, but the tax being remitted by the taxpayer would not take

this into account whatsoever, and the Department of National Revenue would pass this information along to another branch of Government who would then honour the claim and we would get control that way without necessarily increasing administrative costs.

THE CHAIRMAN: That would not take care of the point which subsidization would look after, which I suggest may be significant. That is, to the extent that tax incentives are permitted, they may operate as some do anyhow, as subsidies, but only to those taxpayers who are profitable; only to those members of the community who have taxable income. Maybe the best place for the expenditure of this sort of thing is for people who are not at the present time making a profit.

I thought you might have amplified that kind of an argument.

MR. CONNELL: I quite agree that the incentives are discriminatory quite often in their application. The fact that you mention is mentioned in paragraph 14.

This vehicle has perhaps a defect because of that feature.

COMMISSIONER PERRY: The argument made is that at least the tax incentive leaves free play of the market. It is up to the company or the individual involved to take the initial step, and therefore you are not inviting Government control.

Quite often just as soon as the Government starts paying directly for something, it wants to control directly too. This is the sort of thing you are inviting.

MR. HARVEY: I think one reason we did not

use the word "subsidy" is because of the connotation placed on it. For example, Mr. Carter, you suggested what could possibly happen is that people with taxable incomes benefit by these incentives, and those without, do not have them. Really we are not attempting to subsidize anybody here.

We are attempting to encourage certain types of economic activity in this country, and as such, I think there is a terrific difference between the two.

COMMISSIONER WALLS: Is it not a fact although you say traditionally the Income Tax Act has been employed for this purpose, really tariff protection with your industry is another form of protection? That it does the same thing in subsidizing the industry.

MR. HARVEY: I think that is probably true, yes.

COMMISSIONER PERRY: I think one result of tabulating the cost of the subsidies that you mentioned here might be the amount would be so niggardly that Parliament would be quite incensed and would double the subsidy.

MR. HARVEY: We won't know until we try.

MR. GLASSPOOLE: What you are saying, Mr. Perry, is that bad if the intent of the legislation is good itself?

COMMISSIONER PERRY: No, I agree. This would assist in a more realistic appraisal of what was being accomplished.

THE CHAIRMAN: You speak of double taxation next. You refer to it further on in your submission

on Page 11. First of all, of course, we are very curious as to whether or not there is double taxation of corporate income -- it is spoken of loosely I would suggest -- to the extent that it is borne by others than shareholders? In the first instance I do not think we have double taxation. It is obviously not uniform, anyhow. But if it were something like 50 per cent of corporation tax being borne by shareholders and the other 50 per cent being borne by others than shareholders, the dividend credit would go a long way to offsetting any double tax, and there would not be any problem.

You suggest that consideration be given to a tax credit to corporations for dividends declared by the corporation.

That is in fact reducing the tax on distributed income and making a wider distinction between distributed and undistributed income I would think, the thought being there that it would lessen the impact of double taxation.

COMMISSIONER WALLS: Why would you suggest that rather than a straight reduction of corporation tax?

THE CHAIRMAN: Reduction would apply to both distributed and undistributed, and you are trying to distinguish between the two are you?

MR. GLASSPOOLE: That is correct.

MR. CONNELL: I think that we feel that the corporate form of enterprize can indulge in business just as the unincorporated form of enterprize, and in the one instance the income is taxed at corporate rates

and then is taxed a second time on the residual amount, but also subject of course to the dividend credit, but in the case of the unincorporated business, this is taxed immediately in the hands of the owners of the business.

If you follow through some of the arithmetic, it can be shown that the net after tax money is less in the case of the shareholder than it is in the case of the individual unincorporated owner.

I think what we would like to see is a restoration of equity as between these various parties whether or not they are incorporated.

THE CHAIRMAN: You would not of course welcome the idea that all corporate earnings be taxed immediately in the hands of the shareholders just as they did in the case of a partnership?

MR. CONNELL: I think this would not be too practical particularly in widely held companies.

THE CHAIRMAN: I think it would not.

MR. CONNELL: So it may be that shall we say some tax is necessary to be placed upon undistributed income of the corporation, pending its eventual distribution to the shareholders, at which time they are liable and should be paying personal taxes, just as anyone else would.

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COMMISSIONER PERRY: One of the major problems here is that something like half the dividends go abroad and where we recoup personal income tax on those going to Canadianswe would suffer a very substantial loss of revenue on those going outside the country.

Do you have any comment on that point?

MR. HUGHES: I think probably our first recommendation, the primary consideration is that the credit beallowed the corporation. This would overcome the problem, would it not?

COMMISSIONER PERRY: I am not sure. This would mean that income which is now being taxed in the future would not be taxed excepting for that withholding rate of 15 per cent, perhaps 20 per cent or 10 per cent, whatever it is. This would represent a loss of several hundreds of millions of revenue.

I could lead you on by saying that other witnesses have proposed there be a 50 per cent tax on dividends leaving the country to maintain the present position on such dividends. Otherwise you would be giving a very substantial subsidy to the Treasury of some foreign country, the taxpayers in those foreign countries no longer having a substantial tax credit to deduct from their tax.

MR. GLASSPOOLE: I think the insertion was to try to circumvent the double taxation that has been talked about. If there were a withholding tax placed by the corporation, which the corporation must make at the time it earned profits, and then that withholding tax in effect was credited back for the amount of dividend

paid and the dividends distributed it would be considered to be income in their hands for which they would get no credit.

That income in the form of dividends which were distributed to non-residents could still be taxed at whatever rate would be equitable based on the current type of tax that the non-resident is already paying on dividends received. That is the intent of the section. It is a single tax approach.

COMMISSIONER PERRY: Non-resident would then be taxed at 50 per cent or some such rate?

MR. GLASSPOOLE: That is right.

THE CHAIRMAN: Is that a practical situation to impose that kind of high rate?

MR. GLASSPOOLE: The equivalent in effect is what we are doing now. We are not suggesting we reduce income.

THE CHAIRMAN: We happen to be in line with just about every country in the world. What do you suggest would change the situation vis a vis everybody else by putting ourselves in a position to have to justify the very high tax with regard to non-residents?

Let me ask you one more question on this matter of what is fair with regard to corporation tax. If corporations were taxed in somewhat the same way, that is a single tax rather than a double tax, I am not sure they are double taxed but we will assume for the sake of the discussion at the moment that they are, supposing we had a corporation with a large number of shareholders with either very low rates of personal tax

or no personal tax, if you like, because they were individuals with a small income or charitable organizations or something that would not have taxable income, under our present system that company would pay ordinary corporation taxes.

If you are prepared to look through the company completely and say the company is nothing but a conduit to the shareholders there would be no taxes collected under those circumstances. Would that be fair? I don't think you people, if you think about it for a while, would be prepared to say "yes, they should be a conduit and there should be no taxes."

Under thosecircumstances you would be putting the large company at quite an advantage over smaller companies which were owned in a different way.

Certainly in the United States when they found they had companies owned by charitable organizations which were exempt from tax because of the ownership they had to modify the law. I don't think it is such a simple matter.

MR. HARVEY: I think there is an argument there and I believe it is fair to say we approached this problem from the point of view that equity, equity in this context meaning double taxation, is unfair, if you like.

I think you have introduced a new concept here in suggesting maybe corporate earnings are not subject to double taxation. I presume this is based on some consideration as to who does in fact bear the burden of corporation income tax, is it the consumer or the

shareholder?

THE CHAIRMAN: I don't know who bears it but everybody we have tried to examine has suggested that neither extreme is correct. It is said that the shareholders do bear some of the corporation tax and the customers and the employees generally bear some.

In regulated public utilities I think it is pretty clear the shareholders do not bear very much and that it finds its way almost directly into the value of the commodity. Of course it ranges throughout but there have been a number of studies made and most of the studies have come out with some kind of percentage. I suppose the mean average of them might be about half. I don't know.

We may have a better opinion as we go on. I don't think we are ever going to come out with one figure and say "this is it for Canada". I don't think this is possible.

MR. HARVEY: No, I doubt it.

THE CHAIRMAN: I would refer you now to page 12: "Incentive features of tax legislation". You favour, I observe, the research and development incentive. You suggest it should be modified so that the base be broadened. Some people have suggested that there should be no base or the base, if you like, be nil so that all such expenditures are eligible for 150 per cent.

Of course the intention of the law was to increase the expenditures and surely if one directs the incentive specifically at an increase it is going

to be more effective than if it is directed at the total; is it not?

MR. GLASSPOOLE: I think the principle base is sound so long as the base itself is proper. There has been a tremendous amount of discussion as you know, Mr. Chairman, in this one year base and a number of companies have been penalized for having the foresight to get into scientific research before the legislation was introduced.

It is unfortunate for certain companies who got into scientific research in a large way and in that particular respect my own judgment is that the legislation is not encouraging the people who had the foresight in the base year to get into scientific research. They are being penalized at the expense of their competition in some cases.

When you refer to increased expenditure I agree with you and I also submit that after careful study it could well be that the so-called current expenditures should be the excess over base so long as that base is a sufficiently lengthy period of time to be a true base.

In the case of capital expenditures it could be no base whatsoever is required for the pure and simple reason that all capital expenditures in the area of scientific research in fact are additional and therefore result in additional efforts in the area of scientific research.

To put it differently all scientific expenditures, not planned as such, are in effect growth

in this area.

THE CHAIRMAN: Thank you. That is indeed an interesting comment.

COMMISSIONER PERRY: I was going to say that this is one of the ironical results of incentive legislation that those who are already doing what is wished done gain nothing by the incentives. It is only those who are not who get something from the encouragement.

MR. GLASSPOOLE: I might comment, Mr. Perry, those organizations who prior to the date of the introduction of the legislation were performing research would not necessarily be upset. If the legislation enacted a base period that did not penalize an organization who in the particular 12 months period mentioned in the legislation saw fit to really go overboard in the area of scientific research, particularly in the capital expenditure field.

To this particular extent I believe that the legislation is not performing what it is intended to perform and that is encouragement to those companies to increase their activities in this area.

THE CHAIRMAN: The next item is: "Special Problems, Non-Deductible Costs." This is a novel approach as far as I am aware to add these things or bring these in as a capital cost with a separate class. We have had many recommendations suggesting that they should be allowed as a straight deduction from income.

MR. HUGHES: Our only thought is this may be more politically expedient than the recommendation you

speak of.'

THE CHAIRMAN: Well, perhaps you are correct. I would like to hope we are not to be influenced by political considerations.

COMMISSIONER PERRY: There would not seem to be much chance of recapture on any of these items.

THE CHAIRMAN: We move back to page 8. I skipped sales and excise tax at that point and I think you must couple page 8 with page 16. "The present provisions of the Excise Tax and Regulations for Payment of Federal Sales and Excise Taxes do not always provide an equitable base for tax." You recommend the basis of change from manufacturing level to the level at which the consumers purchase goods. Mr. Walls has a question there.

COMMISSIONER WALLS: First of all I would like to know whether in your recommendation you are giving consideration to a visual or a hidden sales tax at the retail level?

MR. HARVEY: I think they are definitely visual.

COMMISSIONER WALLS: What then led you to believe the provinces would agree to this and to accomplish it would be prepared to adopt common conditions and common exemptions.

MR. HARVEY: I suppose historically nothing would lead us to believe this could happen.

MR. HUGHES: Except I think is it not a fact that the provinces much more recently have introduced the provincial retail tax, have been more inclined to parallel conditions in the Federal Act.

COMMISSIONER WALLS: I don't know whether they parallel the Federal Act. There is a wide variation in exemptions and what is covered in all provincial sales tax legislation. The point I am getting at is this: supposing the provinces will not go along with a combined tax would you still recommend a visual Federal Sales Tax over and above the Provinces Sales Tax?

THE CHAIRMAN: Do you think we should recommend to the Federal Government irrespective of what the Provinces do? We have nothing to do with them. The Federal Government imposes a kind of tax Mr. Walls suggests.

MR. HUGHES: I would agree it would be certainly very, very desirable to have these combined for the simplicity of administration.

COMMISSIONER WALLS: If the Federal Government had to go it alone would they still make it a visual tax?

It would now have to show to the retailer so many cents on the dollar for the Federal Government and so many cents on the dollar for the Provincial Government. You would still make both taxes visual, would you?

MR. GLASSPOOLE: I think the point is, Mr. Walls, one would like to close one's eyes and dream and there would be one tax and the sharing of the tax revenues as such would be between the governments concerned.

COMMISSIONER WALLS: I recognize that is the idea. I am asking you if you feel it is possible. If it is not possible what is the alternative? We will have

to consider that as we have no power over the decisions of the Provincial Governments or no authority in this Commission for considering the plan they should take.

MR. GLASSPOOLE: We believe this is ideal and any efforts on the part of the Commission we would respectfully hope would be directed towards this ideal. While one can readily admit it may be many, many years away and there is a lot of toil to come, it must come before we reach that ideal situation, nevertheless in the long term and in the interest of cost reduction in the form of administrative costs this is the ideal and we should be channelled towards that ideal.

COMMISSIONER WALLS: As far as administrative cost is concerned there would probably be no sales tax put into effect any lower than the one we have got. From the standpoint of administrative costs.

MR. GLASSPOOLE: From the Federal point of view, yes. I am concerned with the Provincial and Municipal taxes, such as in the Province of Quebec. I am sure one can readily state that the total cost of all these consumption taxes or sales taxes, as the case may be, could be reduced.

MR. HARVEY: I don't know I quite appreciate your point, Mr. Walls, where you are stressing should it or should it not be a visual tax. I think our feeling here to a certain extent anyway is this should be a visual tax. People should be aware of what the cost of central government really is and for that reason we believe it should be a visual tax. I think you are attempting to make some distinction there.

COMMISSIONER WALLS: We have had people that have represented the same idea you are making right now and those who believe it should be a hidden tax. You say it represents to them what the Government is costing them. It doesn't. All it does is show they are paying so many cents extra to two Governments on that particular article.

That is not letting them know what Governments cost.

MR. HARVEY: It makes them aware of the fact the Government is costing them something.

COMMISSIONER WALLS: You don't think they know that now?

MR. HARVEY: I have no doubt they realize it but when you go through successive election campaigns and more and more promises maybe there is some lack of understanding of the cost of these promises.

COMMISSIONER MILNE: I want to direct this to Mr. Glasspoole. In relation to your comment I believe I understood you to say you felt the cost administratively could be reduced with the application of the general type of tax. If we can give any credence to certain areas of reporting it seems to me that just very recently I saw something that related to many millions of dollars of retail tax which is due to the Provincial Governments on which there seems to be difficulty collecting.

Now do you think there would be a possibility that in this particular area that type of problem would cause a very great increase in administrative cost.

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MR. GLASSPOOLE: When you refer, Mrs. Milne --

COMMISSIONER MILNE: I think it referred to Quebec, but I could be wrong on that.

MR. GLASSPOOLE: I do not know the specific article to which you are referring, but it seems to me that if the law was to indicate that there was a so-called retail tax collectible at retail level, it certainly would be apparent the Government concerned in its collection should ensure it is collected.

COMMISSIONER MILNE: Is this not administrative cost? Do you think there is a possibility of this being almost a monster if millions are slowly coming in?

MR. GLASSPOOLE: I am not aware of the comments to which you are referring which indicate that retail taxes as such, are not being collected to the extent that the law provides.

COMMISSIONER MILNE: I did precede this with the comment "if we could give credence to certain reporting".

COMMISSIONER WALLS: Going back just briefly to the standpoint of the tax at retail level, do you think it is going to be acceptable to the consumer to have to face up to the size of tax? In other words, you are going to have of the 11 per cent brought forward to the retail level, about 8 per cent, and you add to that the 5 per cent in provincial tax existence; you are then faced with 13 per cent combined sales tax.

Also with Provinces looking for additional revenue, and already in that field, and many of them already considering it their sole field, that tax could

go up to a considerably higher percentage, and that is why I wondered how acceptable it is going to be to the consumer.

MR. GLASSPOOLE: In our deliberations in the making up of this brief, there was not unanimity of thinking with respect to a so-called direct tax recommendation.

COMMISSIONER WALLS: I see. Then going on to some of your other recommendations, you of course also deal with this sales tax on machinery and apparatus of production, and suggest it be repealed. It is estimated when that reaches 11 per cent it is going to bring in revenue of at least one hundred and forty million dollars. Where would you suggest that we alternatively find that one hundred and forty million dollars?

MR. HARVEY: I don't think we could suggest an alternative per se. Once again I suppose we could only speak from what we consider to be the standpoint of equity, and once again this gets into the area of double taxation and so on, and this maybe comes back to direct taxes as well.

It seems to me that since corporations do not vote, that maybe this is an area where it is a little easier, like politically, to raise tax revenues. Whether justice is being served in that sense I suppose is questionable.

COMMISSIONER WALLS: I mentioned one hundred and forty million dollars, but based on the second half of tha same recommendation, it would be a great deal more because you now want it also to apply to the materials

that indirectly go into production. I presume by that you are referring to trucks, office equipment, office furniture.

MR. HARVEY: I do not think we were going to the extent of office furniture and that type of thing. I think we were speaking of ancilliary equipment, if you like, in the production facility as such.

COMMISSIONER WALLS: How would you define materials that indirectly go into a product? We have enough trouble right now to get a list of those that directly are used either on the exemption list or non-exemption list, but if you get into where a product is indirectly used, how are you going to define it?

MR. HUGHES: I do not think that is as difficult as it sounds, Mr. Walls. I think we have visions here of anything going into the office of the plant -- any expense prior to the cost of distribution.

COMMISSIONERWALLS: In other words, taking your own example you would have certain office furniture connected with your firm that is taxable and certain that is not taxable?

MR. HUGHES: Yes.

COMMISSIONER WALLS: I think that would lead to a great deal of administrative difficulty.

MR. CONNELL: It may be your question begs another question. Perhaps the same treatment should be accorded to distribution channels as well, and again depending more on the ultimate consumer's tax as being a source of revenue.

COMMISSIONER WALLS: In other words, if you

move this tax forward to the retail level, you mean it is quite possible the office furniture would have been bought as a retail purchase and be taxed?

MR. CONNELL: No. In other words, the distributor would purchase office equipment perhaps free of tax because the end product that he was distributing would be taxed in terms of ultimate consumption rather than as a process in getting the product to the market.

COMMISSIONER WALLS: I think you are now looking at something over two hundred million.

MR. CONNELL: I think in regard to this tax on production machinery and equipment, it is a remarkable imposition of tax in the light of the great emphasis that seems to have been placed recently on the importance of the Canadian manufacturing industry. This simply serves to increase the cost of production, and this, particularly in the export business, will tend to reduce competitiveness in terms of cost price competitiveness.

COMMISSIONER WALLS: Has your industry worked out any figures that will suggest how much it will increase your export prices?

MR. CONNELL: If I may answer this another way: as far as our own case, I would say the cost of production is increased in the order of perhaps 2/3's of 1 per cent, in that general area.

COMMISSIONER WALLS: With that 2/3's of 1 per cent, that must mean machinery is a relatively high factor in your cost; is that right?

MR. CONNELL: It is of considerable importance. It is perhaps not as great as in some others; for example,

the utility business that some reference has been made to, but with the rate of 11 per cent, this is a fairly high rate and the effect is quite substantial.

MR. GLASSPOOLE: You raised the query, Mr. Walls, if the Government vacated this field of taxation on production machinery and so on that when the cut does become 11 per cent, they will be vacating $140 million per annum.

I do not think what we are saying here, we are opposed to raising an additional hundred and forty million from the sales tax vehicle itself, but what we are opposed to is inequities that exist when sales tax is applied to production machinery because goods which come from the machines are in effect also taxed and we believe that this is unfair.

Further to what has already been said with respect to exports, we believe that it creates an inequity with respect to competing imports as well.

COMMISSIONER WALLS: I would estimate then if this were taken off, and also taken off the indirectly used materials, you would then have to increase this retail sales tax in order to cover that -- if that is the medium you are suggesting -- by another two percent so then instead of thirteen ~~cents~~ percent you would now be charging fifteen ~~cents~~ percent tax to the consumer.

However, I think we have pursued this about as far as we can at the present time. The next thing is inequitable treatment of the wholesalers. I presume what you are dealing with there is inequity between unlicenced wholesalers and licenced wholesalers because

the unlicenced wholesaler pays sales tax on receipt of goods based on his cost from the manufacturer or of import. On the other hand, the licenced wholesaler pays his sales tax when he sells the goods although it is also based on the cost from the manufacturer or of import.

Now, have you considered how both wholesalers might pay sales tax from the time they sell the goods as an alternative to your suggested retail sales tax? This would get you away from this difficulty entirely? In other words, have you considered a wholesale tax?

MR. HUGHES: I think generally we felt that the same problems that are now in existence will just move forward one step.

COMMISSIONER WALLS: No, you would no longer have any difference in treatment of a licenced or un-licenced wholesaler. In fact, there would no longer be a need for them, and the only difference then would be that the tax would be on the cost to the retailer instead of on the selling price of the retailer, and you would remove these anomalies that you have between the manufacturer and wholesaler, or in some cases, between the manufacturer and the retailer.

THE CHAIRMAN: And the importer.

MR. HUGHES: We have to consider that in connection with the point about bringing tax out into the open for the consumer. Secondly, and I do not want to labour that last point, but you mentioned the rate of tax which would be necessary at the consumer level versus the present rate.

Is there any basis in fact for these rates you mentioned? I don't know. I am of the opinion that it would not be in the area which you suggest, because at the present time you have a mark-up on the tax itself at the retail level.

I lean more -- although I cannot substantiate this -- I lean to the theory that at the consumer level the tax applied at the consumer level would mean what you as an individual take out of your pocket to pay for an article would be less than at the present time.

COMMISSIONER WALLS: Well, the figure of 8 per cent that I used was arrived at by an authority on taxation, and he did it on the presumption that there was pyramiding. If there is not pyramiding,it would be more than 8 per cent.

MR. HUGHES: There is pyramiding.

COMMISSIONER WALLS: But it all depends on the degree, and he did it on the basis that in all cases it was pyramided. If it is not pyramided, it would perhaps require more than 8 per cent.

MR. HUGHES: I am suggesting it would require less.

COMMISSIONER WALLS: I don't think so. However, I can only go on figures that have been arrived at by people who are a little more expert than I am.

MR. HUGHES: Thank you very much, sir.

COMMISSIONER WALLS: The next item you deal with is exemption certificates, responsibility for assessing validity of the exemption certificate. Of course Section 68 of the Act states that where a purchaser

makes false representations to the manufacturer that the goods are for exempt use, the manufacturer has the right to recover from the purchaser. I cannot find in the Act where it gives the manufacturer much power to get that back. I presume that is why you wish the purchaser to be directly responsible. Am I right in this case?

MR. HUGHES: If I may add a comment there, Mr. Walls, I presume you have read the recent Skuttle Manufacturing case. The reference is 1963, D.T.C., 1314.

THE CHAIRMAN: The name of the case was Skuttle?

MR. HUGHES: Skuttle. The essence of this judgment, and I do not know whether the judgment has been appealed and I would think it would be, the essence of the judgment is that you are not protected when you have improperly worded certificates, so that I think we are in agreement we would like this recommendation to be enlarged to say that the Act should be amended to hold them wholly responsible for the payment of tax.

COMMISSIONER WALLS: Of course the purchaser in many cases is not a tax payer in the sense of the sales tax. It would be hard for the Government to recoup the tax from somebody that they are not already doing business with in that particular tax field. The only thing I can see from reading the Act is that there should be some more power given to the manufacturer to be able to force the purchaser to recompense them.

All the Act appears to say is that he has the right to get it back from the purchaser.

MR. HUGHES: Of course the objection we have

is that you may in some cases recover the tax, but you are hardput to recover interest penalties from the customer.

COMMISSIONER WALLS: I see justification in your case.

MR. HUGHES: We believe that anyone who certifies something should be held responsible for that certification. I am not aware of any other Act under which a person giving a certification is not held responsible for that certification.

COMMISSIONER WALLS: Except under Provincial sales tax where they operate exactly the same way.

MR. HUGHES: We find the Provincial Governments in their administration are much more lenient than the Federal Government.

COMMISSIONER WALLS: Then we will go on to this administration in regard to departmental rulings where you suggest that they be published in the Canada Gazette. Just for my own edification, I presume at the present time the practice is only to send out departmental rulings that directly affect the manufacturer concerned. In other words, they are not going to send out rulings that pertain to, let us say, the boot and shoe business to people in the electrical industry, and yet you would like them to do that so that you would have some guidance as to what the other fellow is getting. Is that what is behind it?

MR. HUGHES: Yes.

COMMISSIONER WALLS: Would it not be just about as easy for them to send out all bulletins to all

licenced manufacturers instead of just the ones peculiar to your industry.

MR. HUGHES: It sounds as though it would be as practical, but I think we feel in actual practice if they were required to be published, there would be more observance of the rules.

THE CHAIRMAN: I am not sure I understand what you mean by rulings. With the continuous flow of letters which go out, it would seem to me quite impractical to put them in the Canada Gazette, but quite practical to send them out to all licencees.

MR. CONNELL: This may be an alternative vehicle. I think basically what we want is proper public knowledge as to the rulings, and whether this other means is more practical, I do not think we are in a position at this moment to say.

COMMISSIONER WALLS: Keeping in mind that the Government is in correspondence with all of you every thirty days anyway. It would seem that every thirty days they could very well send you copies of all rulings that they happen to make in that period.

MR. CONNELL: The mere effect of wide distribution would in fact make it public knowledge.

THE CHAIRMAN: I have a few questions left over. Some of your products are subject to excise tax and sales tax. If you move to the retail level, how would excise be imposed? It would be shown and added on at the retail level presumably, so that whatever the rate might be, that would result. Am I correct?

MR. HUGHES: I would think we should give

the same treatment to the excise tax as to the sales tax.

THE CHAIRMAN: You would not do what they do in the States; namely, put it on at some other level. Excise, of course, could be imposed at a different level, but your thought is probably it should be at the retail level.

MR. HUGHES: That is a personal observation.

MR. CONNELL: I think it probably should be removed, and this would remove the problem.

THE CHAIRMAN: My question must, of course, be correct, subject to it not being removed.

MR. CONNELL: Yes. I think following the principle that excise tax, if it were to remain, should be likely put at the retail level.

COMMISSIONER WALLS: Some of the products such as cigarettes are also subject to excise duty.
3 Would you carry that forward too? If so, are you not going to face up the consumer with a terrible shock? Maybe that would discourage smoking and Miss LaMarsh would be quite happy.

THE CHAIRMAN: That is the next question I have here. Just how high can a disclosed sales tax at the retail level go? In France, as you probably know, they have indirect tax of 25 per cent. It does not appear at the retail level. It is collected at all levels, but it is done in such a way as to avoid pyramiding and comes out at 25 per cent, but I do not think they could put on a 25 per cent tax at the retail level and disclose it.

They probably would not think they could do it without disclosure, although I think it might make a difference.

If Mr. Walls' authority is correct that this equates to 8 per cent, and we have 5 per cent or 6 per cent at the Provincial level, and 13 or 14 per cent total, is that not getting up to about the top, or do you think there is any such limit? I suggest to you that more can be collected if it is staged at different levels than from one level.

MR. CONNELL: I think there could very well be a psychological problem in the movement of a retail sales tax in total at the moment. I would suggest that perhaps the transitional procedure would be better where you gradually move this 11 per cent rate, translate it into a retail rate, but only impose it in stages. In other words, you would reduce your earlier tax rate commensurate with the amount imposed at the retail level. If it is 8 per cent -- let us assume it is 8 per cent retail. 11 per cent imposed earlier, and perhaps you take it in four stages of 2 per cent so that you do not have the immediate psychological impact of an 8 per cent amount being placed at the retail level.

THE CHAIRMAN: Then you would have two collection machines?

MR. CONNELL: You would have to during this transitional period, but isn't one of the big features about taking tax here at this level the fact that it appears to be so large?

The only way we have of bringing home to the

public the costs of some of the things that the public are demanding - where do we end as far as continued growth of public expenditures? How much can business and the country stand in the way of these expenditures?

THE CHAIRMAN: Well, we in Canada are taxed something like 25 per cent of our gross national product. There are other countries running a great deal higher than that. Yet we do feel that our taxes are pretty high. They seem to be pretty high at the corporate level; pretty high at the personal income tax level, and certainly our sales, when you put the two together, is a good high tax.

At the same time, as I say, you have many who are carving off more than 25 per cent of the G.N.P.

I do not know whether we could achieve those levels unless we do some of the things that the other countries do, and that is not making it absolutely clear as to just where the taxes are paid.

As I say, in France they do not make it very clear, and they are pretty lenient in regard to personal income tax. Perhaps that is how they get all the taxes they do. I don't know, but I would have thought if one imposed a very high tax at the retail level, it would certainly be a motivation for all kinds of pressures for exemptions and so on. Maybe that is desirable, I don't know.

MR. HUGHES: If a tax is being collected, if there is justification for it being collected, what is the objection to showing it separately? Is it just the psychological reaction?

THE CHAIRMAN: I think so. In one country I have seen they have a law prohibiting it being shown separately. I suppose that is understandable. The politicians would prefer that it not be shown.

MR. HARVEY: I wonder if part of our problem here -- in your terms of reference I know you have to raise sufficient tax dollars to cover national expenditures. I think our approach to this problem maybe isn't in keeping with your terms of reference to a certain extent, because I believe we are in effect suggesting here a lot of people know what they are paying, and this then should exert some pressure on the Federal Government to look far more closely at the national expenditures than right now.

Maybe this is a naive assumption, I don't know, but I think this type of thinking is underlying what we are thinking here.

You people, on the other hand, have a different problem. You have got to raise sufficient tax revenues to meet whatever the expenditures may be. However, I do not think that the other side of the problem can really be completely ignored.

MR. CONNELL: This doesn't actually indicate the position of tax at the retail level. If it were decided that rather than show it as a separate addition, it might very well be built into the price that you pay, and the calculation is relatively simple.

THE CHAIRMAN: That is certainly an alternative there is no doubt.

MR. CONNELL: But I think, having tax imposed

at this level, we believe gets around a number of inequities and problems.

THE CHAIRMAN: I would have thought were it not going to be done at the retail level, rather than assess it on the price that the retailer sells his goods for, one might assess it on the amount which he pays for his goods, and that would reduce the cost of collection very, very substantially, but of course it would not provide for as equitable a tax as it would if it were on the selling price, because the closer one gets to the consumer, the better one achieves equity.

MR. CONNELL: There are some inequities in the channels of distribution.

MR. HUGHES: That is the point at which you come closest to equity, at the consumer level.

THE CHAIRMAN: It is also the most expensive point to collect it.

MR. HUGHES: Is this the fact?

THE CHAIRMAN: I think so. It has an awful lot more outlets.

MR. CONNELL: You are dealing with more sources of collection.

THE CHAIRMAN: Many more.

MR. CONNELL: Every level of taxation -- for example provincial taxes -- if those could be combined in their collection perhaps in total, as Mr. Glasspoole suggested, the total cost of collecting the tax in fact would be lower.

COMMISSIONER WALLS: One other angle, of course, is the percentage of bankruptcies at the retail

level is quite high, and the Government already has taken considerable loss even at the manufacturer's level in back taxes that have been collected and not paid. In the retail level you would encounter a great deal of that problem.

MR. HUGHES: While we have not settled this, I think it is our feeling -- perhaps I am wrong, gentlemen -- that we are not opposed to the application of consumer tax to services except as they affect the cost of production.

THE CHAIRMAN: Thank you. You have not discussed that in any great detail I take it because of course the immediate question is what do you mean by "services"? I do not think unless you have gone into it at some length it is worthwhile getting into it because it poses a number of problems as you can see.

Thank you very much, gentlemen. This has been an interesting morning for us. You have given us a great deal to get on with, and we will continue to ponder what you have put before us. Thank you very much.

3 MR. SAMIS: Mr. Chairman and gentlemen, I want to thank you for the very cordial reception you have given us here this morning, and also for the interest and attention which you have shown in our views.

THE CHAIRMAN: We will stand over until 9:30 tomorrow.

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